1983 BUDGET REQUEST OF THE SMALL BUSINESS ADMINISTRATION

HEARING

BEFORE THE

SUBCOMMITTEE ON SBA AND SBIC AUTHORITY, MINORITY ENTERPRISE AND GENERAL SMALL BUSINESS PROBLEMS

OF THE

COMMITTEE ON SMALL BUSINESS HOUSE OF REPRESENTATIVES

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FISCAL YEAR 1983 BUDGET REQUEST OF THE SMALL BUSINESS ADMINISTRATION

THURSDAY, FEBRUARY 25, 1982

HOUSE OF REPRESENTATIVES, SUBCOMMITTEE ON SBA AND SBIC AUTHORITY, MINORITY ENTERPRISE AND GENERAL SMALL BUSINESS PROBLEMS, COMMITTEE ON SMALL BUSINESS,

Washington, D.C.

The subcommittee met, pursuant to notice at 1:30 p.m., in room 2359-A, Rayburn House Office Building, Hon. Parren J. Mitchell (chairman of the subcommittee) presiding.

OPENING STATEMENT OF CHAIRMAN MITCHELL

Mr. MITCHELL. The hearing will now come to order.

Today we are holding hearings to receive supportive material from the Small Business Administration on the Administration's budget request. There are two such requests: further reductions in the 1982 budget, and more reductions in 1983.

Usually I would take this opportunity to summarize the major provisions in the budget request and then listen to the SBA's rationale before forming my opinions. In this case, however, try as I might, I cannot do so. I have examined and reexamined the Administration's budget request. There is nothing in it—I repeat, nothing in it which is good for the small business community. In one word, it's outrageous, simply outrageous.

Everyone knows the state of our economy and that it continues to worsen. Last year Dun & Bradstreet reported that there were 17,000 business failures, the second highest number of business failures in 35 years; the number of failures continue to escalate this year. If this rate continues, there will be 5,000 more failures, small business failures, this year than last year.

In these perilous times, one would expect the Administration to provide more financial assistance, especially it should be expected from an Administration which professes to believe in job creation in the private sector. Instead, the Administration is proposing exactly the opposite. It proposes to eliminate the direct loans to the handicapped, to minorities, for energy conservation, and to others who are unable to obtain funds from any other source.

The Administration also proposes to reduce bank guaranteed loans.

This Congress, in which I serve, appropriated funds for $4.5 billion in guaranteed loans in 1981. Last year, as a part of the

Administration's spending reductions, this amount was reduced to $3.3 billion for 1982. That's a cut of 27 percent.

Now, this year, the Administration wants the level cut by another 17 percent during the remainder of this year, and it proposes to reduce the bank loan program by another 12 percent in 1983. That's why I say this request is outrageous; one of the reasons why I say it.

Even this 47-percent cut in only 3 years is not enough. Even larger cuts are planned in the future so that by 1987 the annual level for bank guaranteed loans will be less than $1 billion.

The picture is worse in other areas. To make matters even worse, the Administration is not even being up front about the extent of the cuts. I have spent a great deal of time with members of the Budget Committee and other Members of Congress. We are not dealing with a $91 billion deficit. We are dealing with a deficit that is real, and the real deficit is about $120 billion. This business of mirrors and shadows to try to sell the public that the deficit is only $91 billion is wrong.

For example, the Administration says it is maintaining minority small business lending at $440 million. That is an absolute and complete sham. Included within this amount are economic opportunity loans. Under existing law, $60 million is authorized in EOL guarantees, and the Administration proposes to increase this to $100 million this year, and to $167 million next year. Now, that looks good, but in 1980 the banks made only $24.5 million in guaranteed economic opportunity loans, and this amount dropped to $20.4 million last year.

The experience to date this year has been even worse. In the first 4 months of fiscal year 1982 the EOL loan guarantees total $2.8 million. If this rate continues, the 1982 total would be $8.4 million. There is a chasm between $8.4 million and this projection of $100 million by the Small Business Administration. Certainly everyone hopes the economy will improve. God knows I do, and I hope the interest rates will decline. This would probably result in an increase in the EOL guarantees, and I expect that will happen. I hope the economy improves. But it is preposterous in my opinion to assert that this program will increase to $100 million in the remaining 8 months—that's an increase of over 1,700 percent—and that the increased rate would not only be sustained next year, but would increase by another 67 percent. That is pure stark, mania madness to make that kind of projection.

I could go on and on, but I won't. We are here to take testimony and I would hope the Small Business Administration will present some rationale for the lack of assistance it is proposing for the small business community. I do not believe we are going to receive anything other than cuts for the sake of cuts. I have vented my spleen. Now let me soften a little bit. The final decision about the budget was made by the former Administrator, Mr. Cardenas, is that correct?

Mr. TEMPLEMAN. Yes, sir.

Mr. MITCHELL. And I assume—and this might be a wrong assumption—but I assume that was pretty much demanded of him by Mr. Stockman. So, gentlemen, while I am angry, understandably angry—and I think you should be, also—I am not really furious

with you because that final decision had been made by Mr. Cardenas. If, indeed, he had been a friend to small business, he would not have accepted this kind of demand from the Office of Management and Budget, and he would not have accepted these preposterously inaccurate projections.

We will have an opening statement from the minority side.

Mr. WEBER. Thank you, Mr. Chairman.

I would like to submit the opening statement that was prepared by Congressman McDade who, as we know, cannot be here today.

OPENING STATEMENT OF HON. JOSEPH M. McDADE, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF PENNSYLVANIA

Mr. Chairman, with this hearing the committee begins its formal examination of the proposed Small Business Administration budget for fiscal year 1983. The proposal contains significant reductions in many cases, but it also offers hope for resolving some of SBA's longstanding serious problems.

I am pleased to note that this budget contains a renewed emphasis on management improvement assistance. In addition, SBA is planning on increasing private sector participation in the management assistance program. I believe that this is essential if this program is to achieve its potential. By making better use of private industry resources, SBA can improve both the counseling and training it offers to small businesses. We are also likely to achieve greater penetration into the small business community through this new approach.

I am also impressed by the management improvements which are proposed in conjunction with this budget. These include greater emphasis on portfolio management, improvements in the Inspector General's capability, a regional management system, and much needed improvements in SBA's data processing capability. These changes should result in a more lean and efficient SBA operation. I am confident that these changes will enable the agency to continue to operate effectively in spite of the cutbacks which are being proposed.

Finally, Mr. Chairman, I would like to commend the Acting Administrator, Mr. Templeman, who is to be our witness today. A transition in leadership, such as the SBA is now undergoing, is always difficult. As Deputy Administrator and as Acting Administrator, Mr. Templeman has given an outstanding performance in leading the agency. It has been a great pleasure to work with him, and I am pleased that he is here with us today to discuss the 1983 budget proposal.

Mr. MITCHELL. Do other members have opening statements? Mr. Addabbo.

OPENING STATEMENT OF HON. JOSEPH P. ADDABBO, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF NEW YORK

Mr. ADDABBO. As you have so succinctly and accurately stated in your opening statement, Mr. Chairman, the Administration has done little if anything as far as small business is concerned. Their magical economic program has fallen completely flat and, unfortu-

nately, the fairytale that was told last year has not ended in any way the way it was supposed to. We see the continued degradation of the Small Business Administration even though the administration knows and has stated on so many occasions how important small business is to our entire economy; that small business represent a large percentage of our business community.

We also know and have seen that all we have received as far as small business is concerned is lip service. Since last January there has not been one single comprehensive statement on small business from this administration.

The administration has insisted that what is good for large business is good for small. That is a nice statement, but in all their actions, including the tax bill, big business has received most of the benefits under the tax bill, and small business has received little. All we see as far as small business is concerned is higher interest rates and recordbreaking bankruptcies, which are wiping out our small business community.

In light of the administration's record last year, it is not surprising that the Administration has again shown its true colors in submitting this inadequate SBA budget. It clearly shows that there is a systematic movement on to practically dismember the Small Business Administration and make it an alphabet only and nothing that can contend with the problems the small businessman sees for himself.

It did not actually begin here. In addition to last year's cuts, we see that the number of employees, even the authorized number of employees, have not been placed on board. You cannot operate an administration or any agency with an inadequate number of personnel. Those who are on board, those who have remained, have tried to do a job, but then there were those who were very qualified, maybe overly qualified—maybe they knew too much about the actions or the operations of the Small Business Administration and through insidious ways were moved out of the agency, whether by force, transfer, or other means. As you know, I and Congressman LaFalce of the General Oversight Subcommittee joined with you in seeking full information as far as these employee transfers, many of which we believe are unnecessary and, most important, caused a waste of much-needed dollars in unnecessary transfers.

As far as the budget is concerned, we have an impossible task of seeking ways to prevent this administration from destroying every Federal program which encouraged small business development.

I have read Mr. Templeman's statement with interest because I think he has the expertise and hopefully still has the will to continue a Small Business Administration and look forward to his testimony.

I assure you, in my other capacity on defense, we are pushing Mr. Weinberger, who says there is some adverse effect on small business on the defense budget because of actions made necessary by our 95–507 set-aside. But as I pointed out to him and his administration, you cannot look at a single item. You must look at the entire budget, at the entire economy, and one part of the economy directly affects another part of the economy. And if the Defense Department has all the dollars, then we must look to them to increase their activities in the small business field, in procurements

and set-asides, because although it might cost them a little at the beginning, we have also found that competition brings down prices. Not only that, it gives better quality, because the men and companies that they've been dealing with, as we read in the newspapers, have not been producing the quality of systems that we need in our military.

So I will carefully listen to the testimony here today. I await the information we are seeking on the personnel changes. Although my work on my other subcommittee may keep me away from these hearings, and away from direct contact with the administration, they will know by hearing from me or through you and our staff, Mr. Chairman, that we are still very strongly interested in a good, strong, viable Small Business Administration because that is the only hope the small businessman has out there.

One thing I will say in closing, one of the things I had great fault with the outgoing Administrator was that he forgot and there are those in the Small Business Administration who do not read the existing law or the law that created the Small Business Administration. The law that created the Small Business Administration provided for direct loans, because that was the basis of the Small Business Administration—to help the small businessman who could not get a loan because for one reason or another, the financial doors were closed to him. Now, we see a complete reversal. So again, working with the chairman and the staff, we will be trying to bring back the Small Business Administration to be not the undertaker of the small business man, but his advocate, which is the role Congress originally gave to the Small Business Administration.

Thank you very much, Mr. Chairman.

Mr. MITCHELL. Thank you for your statement. You are a very, very valuable member of this committee and have served it well.

Are there any other opening statements? If not, Mr. Templeman, we will hear from you.

TESTIMONY OF DONALD R. TEMPLEMAN, ACTING ADMINISTRATOR, SMALL BUSINESS ADMINISTRATION, ACCOMPANIED BY EDWIN T. HOLLOWAY, ASSOCIATE ADMINISTRATOR FOR FINANCE AND INVESTMENT; HARRY S. CARVER, CONTROLLER; AND ROBERT WRIGHT, ASSOCIATE ADMINISTRATOR, MINORITY SMALL BUSINESS AND CAPITAL OWNERSHIP DEVELOPMENT

Mr. TEMPLEMAN. Thank you, Mr. Chairman, and members of the committee. I am pleased to have this opportunity to appear before this committee to discuss the administration's 1983 budget request for the Small Business Administration.

I am accompanied today by Edwin T. Holloway, Associate Administrator for Finance and Investment, Robert Wright, Associate Administrator for Minority Small Business and Capital Ownership Development, and Harry S. Carver, controller.

Mr. Chairman, we consider SBA's budget request to be consistent with the interests of the Nation's small business. In talking with a wide variety of small business people from all geographic regions of the United States, it has become increasingly obvious to me and my colleagues that the top priorities for small business owners are:

improved access to private credit, reduced interest and inflation rates, stable financial markets, regulatory reform, and tax reduction.

SBA, in its role as the Nation's advocate for small business, continues to speak out on these issues and endeavors to insure that small businesses are well represented when Federal policies in these areas are determined. Through our agency's partnership with the private sector financial institutions, we are encouraging private small business financing as well as assisting small businesses in establishing good working relationships with private sector institutions. Whether through our certified lenders program, Minority Enterprise Small Business Investment Company assistance, and Small Business Investment Company assistance, development companies or sureties, this agency is leveraging private sector capital and expertise with Federal resources to assist the small business community.

Most importantly, however, Mr. Chairman, SBA willingly participates in the administration's efforts to bring excessive Federal spending, deficits, and market involvement into perspective. Moreover, we believe that SBA can make a significant contribution to the economic recovery program without significantly retarding our efforts to achieve the agency's mission of assisting the Nation's small businesses.

This can be accomplished by a number of vehicles, including: strengthening the management and control of agency programs and support functions, improving management systems, limiting credit assistance to valid cases of unavailability of credit from conventional sources, and improving the quality of loans approved, combined with intensifying our emphasis in the area of debt collection. Debt collection is important not only from a fiscal perspective, but is necessary to overcome any erosion of confidence in the agency's ability to manage its lending programs and prevent losses.

It is important to note here that most of the management initiatives I have just mentioned are already in the process of implementation—not just to get in line with budget reductions, but because they are and have been for some time necessary for SBA to effectively accomplish its mission.

In the final analysis, it is the success of this administration's economic policies which will allow us to address the small business priorities I mentioned above.

A major component of the administration's overall program for economic recovery is to reduce Federal intervention in the Nation's financial and credit markets. Consistent with this goal, SBA determined that, with the exception of purchasing preferred stock and debentures in MESBIC's, we would request no funding for direct loans in fiscal year 1983.

This is, of course, a major shift in agency operations. It should not, however, be viewed as contrary to the best interests of the small business community as a whole. This committee is very familiar with the history and operation of SBA's direct lending programs. You are familiar with the difficulties associated with establishing "acceptable" loss rates and other parameters for these programs, and with the inordinate resources which the agency has devoted to loanmaking. Additionally, SBA has always had the prob-

lem of allocation of scarce direct loan resources among competing interests. Attempts to utilize various alternative methods of allocation always have resulted in giving one group or business a competitive advantage to the detriment of other small firms.

Mr. Chairman, I recognize there may be small firms operating today who would not be in business without the assistance provided by an SBA direct loan. However, in a time of budget restraint, these funds leveraged through the private sector could provide assistance to a far greater number of businesses, at much less cost in terms of the agency's resources required to administer the programs. Through increased cooperation with private sector financial institutions, as I have outlined above, we intend to still assist those businesses that have a reasonable prospect for success.

By eliminating funding for subsidized direct loans, SBA can turn its attention to other initiatives. Certainly, limiting Federal credit assistance will cause the amount of available private capital to expand and will contribute to a reduction in interest and inflation rates. Consistent with this administration's policy, we are also recommending a reduction in the level of guaranteed lending.

Seventeen percent, or approximately $410 million, of SBA's guaranteed loans in 1983 will be made available for firms owned by socially and economically disadvantaged individuals, as compared with an average over the past 5 years of 9 percent minority participation in the agency's guaranteed loan programs, and 12.8 percent minority participation in all the agency's loan programs, including direct and guaranteed. Also, Mr. Chairman, the certified development company, or so-called 503 program, continues to certify development companies, thereby increasing the private sector share of small business lending in this program which seeks to create significant additional employment.

Clearly SBA's contribution to the effort to reduce Federal intervention in the credit market will not be undertaken at the expense of those who are most in need of the financial assistance that the agency can provide—the victims of market imperfections and discrimination.

While it is important that the committee understand our reasons for reductions in financial assistance, it is even more important that you recognize our commitment to improving the delivery of nonfinancial assistance to small business, with greater emphasis on cooperation with non-Federal Government delivery mechanisms.

We believe that we can continue to deliver optimal levels of nonfinancial assistance to the small business community at the funding levels requested in the budget, and we believe we can do so more effectively and efficiently than has been done before. We do not believe that the proposed personnel reduction will prevent us from maintaining current delivery levels. Management improvements and increased private sector involvement and participation are expected to close the gap of funding reductions.

Additionally, in the area of small business contracting with the Federal Government, this agency, with the statutory support of Public Law 95-507, is having a tremendous impact on the small business community. We have recently completed negotiations with Federal agencies on small business procurement goals for fiscal year 1982. If agencies achieve these negotiated goals, small busi-

nesses will receive $3 to $3.5 billion more in Government contracts in fiscal year 1982 than in 1981. This should push the total amount of Federal procurement dollars going to small business over the $40 billion mark in this fiscal year. These contracting dollars provide real income and have a substantially greater impact on the health of the small business community than providing additional debt capital.

Mr. Chairman, let me assure you that the Small Business Administration intends to continue to be the Nation's primary and strongest advocate for small business; that the Small Business Administration will continue in its efforts to insure that small business receives its fair share of Government procurement; that the Small Business Administration will continue to provide necessary financial and management assistance to the Nation's small business community; and that the Small Business Administration will continue to be an effective tool for minority business development.

In conclusion, Mr. Chairman, we believe the budget request for the Small Business Administration which you have before you is reasonable. Moreover, we believe that we can improve the quality of our service to America's small business community in fiscal year 1983.

Most importantly, however, we feel that small business on the whole in this country will benefit more from our contribution to stable financial markets, interest and inflation rate reductions, and limiting Federal credit assistance, than from our efforts to assist a necessarily limited proportion of this number through increasing programmatic outlays. We support the administration's economic recovery program and we believe we can effectively and efficiently accomplish the mission of the SBA at the reduced funding and personnel levels.

Mr. Chairman, I wish again to express my appreciation for your invitation and for providing us the opportunity to appear here today. We will answer whatever questions you or members of the committee may have.

[Mr. Templeman's prepared statement and attachments follow:]

PREPARED STATEMENT OF DONALD R. TEMPLEMAN, ACTING ADMINISTRATOR, SMALL BUSINESS ADMINISTRATION

Mr. Chairman and Members of the Committee, I am pleased to have this opportunity to appear before this Committee to discuss the Administration's 1983 budget request for the Small Business Administration. I am Donald R. Templeman, Acting Administrator of SBA, and with me today are Edwin T. Holloway, Acting Associate Administrator for Finance and Investment, and Harry S. Carver, Controller.

Mr. Chairman, we consider SBA's budget request to be consistent with the best interests of the nation's small businesses. In talking with a wide variety of small business people in different business classes and from all geographic regions of the United States, it has become increasingly obvious to me and my colleagues that the top priorities for small business owners are: improved access to private credit, reduced interest and inflation rates, stable financial markets, regulatory reform, and tax reduction.

SBA, in its role as the nation's advocate for small business, continues to speak out on these issues and endeavors to ensure that small businesses are well represented when Federal policies in these areas are determined. Through our Agency's partnership with private sector financial institutions, we are encouraging private small business financing as well as assisting small businesses in establishing good working relationships with private sector institutions. Whether through our certified lenders program, Minority Enterprise Small Business Investment Company Assistance, Small Business Investment Company Assistance, Development Companies, or Sure-

ties, this Agency is leveraging private sector capital and expertise with Federal resources to assist the small business community.

Most importantly, however, Mr. Chairman, SBA willingly participates in the Administration's efforts to bring excessive Federal spending, deficits, and market involvement into perspective. Moreover, we believe that SBA can make a significant contribution to the Economic Recovery Program without significantly retarding our efforts to achieve the Agency's mission of assisting the nation's small businesses.

This can be accomplished by using a number of vehicles, including: Strengthening the management and control of Agency programs and support functions, improving management systems; limiting credit assistance to valid cases of unavailability of credit from conventional sources, and improving the quality of loans approved, combined with intensifying our emphasis in the area of debt collection. Debt collection is important not only from a fiscal perspective, but is necessary to overcome any erosion of confidence in the Agency's ability to manage its lending programs and prevent losses.

Mr. Chairman, it is important to note here that most of the management initiatives that I have just mentioned are already in the process of implementation—not just to get into line with budget reductions, but because they are, and have been for some time, necessary for the Small Business Administration to effectively accomplish its mission.

In the final analysis, it is the success of this Administration's economic policies which will allow us to address the small business priorities I mentioned above.

A major component of the Administration's overall program for economic recovery is to reduce Federal intervention in the nation's financial and credit markets. Consistent with this goal, SBA determined that, with the exception of purchasing preferred stock and debentures in MESBIC's, we would request no funding for direct loans in fiscal year 1983.

This is, of course, a major shift in Agency operations. It should not however be viewed as contrary to the best interests of the small business community. This Committee is very familiar with the history and operation of SBA's direct lending programs. You are familiar with the difficulties associated with establishing "acceptable" loss rates and other parameters for these programs, and with the inordinate resources which the Agency has devoted to loan making. Additionally, SBA has always had the problem of allocation of scarce direct loan resources among competing interests. Attempts to utilize various alternative methods of allocation always have resulted in giving one group or business a competitive advantage to the detriment of other small firms.

Mr. Chairman, I recognize that there may be small firms operating today who would not be in business without the assistance provided by an SBA direct loan. However, in a time of budget restraint, those funds leveraged through private sector lenders could provide assistance to a far greater number of businesses, at much lesser cost in terms of the Agency resources required to administer the programs. Through increased cooperation with private sector financial institutions, as I have outlined above, we hope to still assist those businesses that have a reasonable prospect for success.

By eliminating funding for subsidized direct loans, and thereby eliminating another type of market intervention, SBA can turn its attention to other initiatives. Certainly, limiting federal credit assistance will cause the amount of available private credit to expand, and will contribute to a reduction in interest and inflation rates. Consistent with this Administration's policy we also are recommending a reduction in the level of guaranteed lending.

Seventeen percent (approximately $410 million) of SBA's guaranteed loans in 1983 will be made available for firms owned by socially and economically disadvantaged individuals, as compared with an average over the past five years of 9 percent minority participation in the Agency's guaranteed loan programs, and 12.8 percent minority participation in all the Agency's loan programs—including direct and guaranteed.

Also, Mr. Chairman, the Certified Development Company (or 503) Program continues to certify 503 companies, thereby increasing the private sector share of small business lending in this program which seeks to create significant additional employment.

Clearly, SBA's contribution to the effort to reduce federal intervention in the credit market will not be undertaken at the expense of those who are most in need of the financial assistance that the Agency can provide—the victims of market imperfections and discrimination.

While I wanted to make sure the Committee understands our reasons for reductions in financial assistance programs, it is even more important that you recognize

our commitment to improving the delivery of non-financial assistance to small business, with greater emphasis on cooperation with non-Federal Government delivery mechanisms.

We believe that we can continue to deliver optimal levels of non-financial assistance to the small business community at the funding levels requested in the budget, and we believe that we can do so more effectively and efficiently than ever before. We do not believe that the proposed personnel reduction will prevent us from maintaining current delivery levels. Management improvements and increased private sector involvement and participation are expected to close the gap of funding reductions.

Additionally, in the area of small business contracting with the Federal Government, this Agency, with the statutory support of Public Law 95–507, is having a tremendous impact on the small business community. We have recently completed negotiations with Federal Agencies on small business procurement goals for fiscal year 1982. If agencies achieve these negotiated goals, small businesses will receive $3 to $3.5 billion more in government contracts in fiscal year 1982 that in 1981. This should push the total amount of Federal procurement dollars going to small business over the $40 billion mark in this fiscal year. These contracting dollars provide real income and have a substantially greater impact on the health of the small business community than providing additional debt capital.

Mr. Chairman, let me assure you that the Small Business Administration will continue to be the nation's primary and strongest advocate for small business; that the Small Business Administration will continue in its efforts to assure that small business receives its fair share of government procurement; that the Small Business Administration will continue to provide necessary financial and management assistance to the nation's small business community; and that the Small Business Administration will continue to be an effective tool for minority business development.

With improved management and administration of these responsibilities, we firmly believe that SBA will become a better advocate, counselor, lender, and business developer, even at these reduced funding and personnel levels.

In conclusion, Mr. Chairman, we believe that the budget request for the Small Business Administration which you have before you is reasonable. Moreover, we believe that we can improve the quality of our service to America's small business community in fiscal year 1983.

Most importantly, however, we feel that small business on the whole in this country will benefit more from our contribution to stable financial markets, interest and inflation rate reductions, and limiting Federal credit assistance than from our efforts to assist a necessarily limited proportion of this number through increasing programmatic outlays. We support the basic tenets of the Administration's Economic Recovery Program, and we believe that we can effectively and efficiently accomplish the mission of the Small Business Administration at the funding and personnel levels proposed.

Mr. Chairman, I wish to again express my appreciation for your invitation, and for providing the opportunity to appear here today. I will answer, to the best of my knowledge and ability, any questions that the Committee wishes to ask.

RESPONSE TO CHAIRMAN MITCHELL'S QUESTIONS ON THE
FISCAL YEAR 1983 CONGRESSIONAL BUDGET

DISASTER ASSISTANCE

As provided in last year's Reconciliation Bill (P.L. 97-35), the Agency is required to re-open certain disaster loan applications.

Question: What has been the Agency's experience as to the number and dollars involved to date and what additional impact are you expecting?

Answer: There were approximately 16,300 disaster loans and applications that required reprocessing. The borrower/applicant in each case was notified in writing of the provisions of the law. Approximately 6,000 borrowers/applicants made an initial affirmative response to the offer of reprocessing. In 4,100 cases the borrower/applicant provided the information necessary to review the case in accordance with the provisions of P.L. 97-35. Of these, 710 requests were withdrawn by the borrower/applicant, 538 cases were declined, 2,234 have been approved (totaling $59.7 million), and 650 (totaling approximately $27.4 million) are still being processed. The remaining approximately 1,800 borrowers/applicants who had initially indicated an affirmative response did not respond to SBA's followup request for additional information.

We anticipate there will be very few borrowers/applicants who will provide the required information who have not already done so.

The same law substantially increased the interest rates on disaster loans made for disasters occurring after the date of enactment.

Question: What change in demand has resulted from these program changes?

Answer: It is premature to evaluate the impact of 97-35 on the disaster assistance program. There have been very few declared disasters with incident dates after August 13, 1981, and therefore the data available is inconclusive.

Question: What disasters are now in process and which have been closed---provide numbers of applications distributed, number returned, number approved, number disbursed, number projected, and supply dollar amounts where applicable, divided into five groups: homeowner with credit, homeowner without credit, business with credit, business without credit, and other.

Answer: We are in the process of compiling this information and will submit it to you at a later date.

Question: Assuming no additional appropriated funds, what disaster loan program level will the Disaster Loan Revolving Fund support for the balance of 1982 and in 1983?

Answer:

Analysis of Disaster Loan Fund
($ in thousands)

FY 1982 Program Level	$640,000
Add: Unobligated Balance, ending	306,372
Total Available for Obligation	$946,372
FY 1983 Program Level	$440,000
Add: Unobligated Balance, ending*	489,092
Total Available for Obligation	$929,092

*Assumes FY 1982 Program Level of $640 Million.

Note: The Agency will initiate an intensive debt collection program which will result in an additional $65 million in loan repayments, over and above the normal amortization for FY 1982 and FY 1983.

Question: What is the status of the disaster cadre?

Answer: As of February 12, 1982, there are 58 individuals serving in the cadre. The Disaster Assistance Division, in conjuction with the Area Directors, is in the process of increasing the cadre. Our target for the cadre is 124 and we hope to complete selections and appointments as soon as possible in this fiscal year.

Question: How many personnel are assigned to disaster function? Separate between disaster loan making and disaster loan servicing.

Answer: As of February 1982, the Agency had 556 personnel assigned to disaster functions. Of the 556 on-board, 351 were performing loan making and 205 were performing loan servicing. The 351 in loan making includes 9 permanents, 58 cadre, and 284 temporaries. We are currently making efforts to staff up to 275 temporary employees in loan servicing.

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LOAN ASSISTANCE

In 1980, SBA provided 6,600 direct loans for $360 million. The 1983 budget zeroes out these loans.

Question: What source will replace these funds?

Answer: We intend to rely upon the private rector to a significantly greater extent. We have streamlined our guaranty procedure, especially through the Certified Lenders Program, so that we are giving faster service to our participating banks. We feel that the legitimate demand from small business borrowers who can demonstrate repayment ability can be met adequately by our guaranty program.

Question: In 1981, the agency allowed $34.2 million in direct financial assistance to lapse. Why?

Answer: This was basically the result of the timing of availability of funds. Our appropriation level was not approved until June of 1981 leaving actually only the final quarter of the year to place a significantly increased direct loan authority into use. Prior to June our authorized level was $269 million or $67 million per quarter. That amount was increased to $325 million or approximately $123 million to use in the final quarter of this year. There was simply an insufficient amount of time to fully utilize these funds.

Question: During the first quarter of FY 1982, the agency only approved $30 million in direct loans of the $47.5 million made available for such period. Why?

Answer: We believe the principal reason for the downturn in loan volume to be the current economic situation combined with continuing high interest rates. Those businesses that have a discretionary need for funds (for expansion, new starts, etc.) are deferring borrowing until such time as they can be more certain of the benefits of expenditures and profits. This is true not only of direct SBA loans, but also guaranteed SBA loans and bank loans not involving SBA.

Question: What amount of 1981 direct loan funds were allotted to region and/or district offices and what amount was approved? Be specific as to each office and identify any program funds held and approved by Central Office. Same as first quarter of 1982.

Answer: See Attachment I and II.

Question: How many direct loan applications were denied in FY 1981 and 1982 due to lack of ability to repay at the approximately 15 percent interest rate which would have had the ability to repay at a 9-14 percent interest rate?

Answer: While we have no way to identify the precise number, we believe that very few applicants would have been approved at interest rates of 9 to 11 percent but declined at rates of 15 percent. This spread is too small to affect repayment ability calulations on a large number of applicants.

SBIC's

The 1983 budget request for SBIC guarantee is $125 million.

Question: Specify the number and dollar amount of previously issued guarantees which mature in FY 1982 and each of the next five fiscal years.

Answer: Maturing guarantees by fiscal year are as follows:

1982 -	$54.2 million
1983 -	154.3 "
1984 -	86.5 "
1985 -	63.5 "
1986 -	56.5 "
1987 -	83.0 "

The above are the totals of guarantees maturing. However, approximately $35 million of the FY 1983 Maturing Debentures are obligations of Licensees which are in liquidation, and there are other licensees who will not want refunding for various reasons. Many may simply be planning to pay off their debt according to the debenture terms and others would not want to "rollover" their debt because of the likely differential in interest rates. Thus, we estimate that refundings actually requested during FY 1983 would amount to less than $100 million. We are presently surveying the licensees involved to get a better estimate.

POLLUTION CONTROL BONDS

In 1982, the administration proposes a reduction of these approvals to $150 million from the current level of $250 million.

Question: What demand for these bonds do you project in each of 1982 and 1983?

Answer: While it is not possible to accurately predict the demand for this program in FY 1982 and 1983, presently there are commitments outstanding totalling $74,658,364 plus additional applications totalling $93,458,384 yet to be processed, all of which have been received during the past eighteen months. A November 1981, informal polling of underwriters and bond issuing authorities in the thirteen States that are the most active in the program revealed that 151 applications totalling $210 million were being processed for submission to SBA. However at the time of the informal poll, consideration was not given as to the effects of limiting financing to nonetax exempt issues.

Question: What has been your experience to date by fiscal year with this program -- number and dollar amount of guarantees, income from all fees, loss experience and projections.

Answer:

Status of
Pollution Control Program
($ in 000's)

Actual FY	Approvals #	Approvals $	Appl. Fees	Guar. Fees	Income On Invest.	Losses
1977	7	4,600	$15	$263	-	1)
1978	18	9,830	37	648	-	1)
1979	46	42,815	82	2,547	-	1)
1980	76	98,590	116	6,593	-	1)
1981	68	100,000	86	8,499	$1,926	1)
Est.						
1982	135	150,000	$130	$12,750	$3,820	$750 1)
1983	135	150,000	130	12,750	6,420	750 1)

1) SBA experienced no losses on Pollution Control in past fiscal years. In the event of future losses the FY 1983 budget request contains a 1/2 of 1% reserve for FY 1982 and 1983.

POLLUTION CONTROL (cont'd.)

Question: We understand that retroactive to January 1, 1982, SBA will not approve any bonds which are planned as tax exempt.

What is your authority for this?

How are you doing it?

What status is it in?

Answer: The authority to guarantee transactions involving both taxable and tax-exempt financings comes directly from the statute P.L. 94-305, Section 404(b)(1)(2)(3). Tax-exempt authority is specifically dealt with in Section 404(b)(1), which states:

"Notwithstanding any other law, rule, or regulation or fiscal policy to the contrary, the guarantee authorized in the case of pollution control facilities or property may be issued when such property is acquired by the use of proceeds from industrial revenue bonds which provide the holders interest which is exempt from Federal Income tax."

We may issue guarantees on taxable financings only through the OMB apportionment of appropriated funding level.

Implementation of the taxable financing guarantee allocation is being accomplished as follows:

-

Letters to all applicants advising them of the change to taxable financing. Requesting them to consider restructuring to taxable and advising us of how they plan to accomplish the restructure.

-

Reprocessing and re-analyzing each respondent to determine creditworthiness and ability to handle the more costly taxable financing.

-

Recommending changes in the program rules and regulations which will reduce the guarantee fee, increase the amount eligible to be financed, provide for principal only unequal payment guarantee to facilitate variable rate financing, and permit the transfer of tax benefits of ownership from the user of eligible equipment to a third party to assist in reducing the overall net interest cost of financing to the small concern.

POLLUTION CONTROL (cont'd.)

Currently, SBA is beginning to receive responses from some applicants requesting processing of their applications on a taxable basis.

The present status of the Pollution Control program since inception through January 31, 1982, has been answered in the previous question.

SURETY BOND GUARANTEES

In 1982 and 1983, the administration proposed total surety bond guarantees of $1,080 million instead of the current level of $1,200 million and last year's $1,400 million.

Question: What demand do you anticipate in 1982 and in 1983?

Answer: Demand for surety bond guarantees is difficult to estimate for both FY 1982 and FY 1983, but average annual demand based on the past five years of program activity amounts to $1.27 billion. The following reflects the past 5 years of activity.

	Guarantees Issued
FY 1977	$ .9 billion
FY 1978	1.2 "
FY 1979	1.4 "
FY 1980	1.5 "
FY 1981	1.4 "

We understand that the administration recently reduced the maximum amount of a bond on which it would issue a guarantee to $250,000 (instead of the statutory $1 million).

Question: Based on program experience, how many contracts will be precluded from surety bond guarantees in each of 1982 and 1983 by this action?

Answer: It is currently estimated that for FY 1982 and FY 1983 we will approve 14,000 surety bond guarantees within a program level of $1.08 billion. FY 1981 actual date reflects 17,821 guarantees of which approximately 93% were approved at $250 thousand or below. Therefore a very small percentage will be excluded due to reducing the maximum amount of a bond to $250,000.

Question: During the first quarter of 1982, SBA approved guarantees of $199 million of the $300 million made available by Congress. Why?

Answer: Beginning in the spring of 1981, the Agency initiated a series of underwriting letters to field offices designed to improve the quality of Surety Bond Guarantees and to bring the program into line with the Administration efforts to control Federal government guarantee activity.

The most recent of these was signed 1/15/82 and set forth two underwriting standards that are having the effect of substantially cutting SBG volume. Contract amount eligible for guarantee was set at $250,000 and no contract could exceed 125% of previously successfully completed work. In addition, the economic conditions and severe weather have undoubtedly impacted on the program demand.

MINORITY SMALL BUSINESS

The budget explanation includes $440 million for minority small business lending. Included would be an increase in EOL guarantees to $100 million in 1982 and to $167 million in 1983.

Question: Since 1982 experience to date, annualized, would result in only $10 million in EOL guarantees in 1982 and since in the two most recent years EOL guarantees were only $24.5 million in 1980 and $20.4 million in 1981, what is the basis for your projected increase?

Answer: The increased amount is based on the Administration's commitment to ensure that minority-owned firms have an equal opportunity for growth and development. The SBA will focus its efforts towards guaranteed loans and will foster the developmment of sound relationships between minority firms and private financial institutions. Specifically, the Economic Opportunity Loan program has an increased funding level to provide available financing to the minority business community, which in the past has experienced difficulties in acquiring financing in the private sector due to the high credit risk perception.

PERSONNEL

In FY 1981, SBA had permanent employment of 4,275. This number would be reduced to 4,036 in FY 1982 and 3,818 in FY 1983.

These reductions amount to more than 10 percent in each of eight areas: management assistance, finance and investment, minority small business COD, advocacy, personnel management, data and management services, equal employment opportunity and compliance, and field management.

Question: For each area, specifically describe the nature of the reduction and its impact upon the activity involved.

Question: Will any of these reductions involve RIFs? If yes, which and how many.

Question: Will any of these reductions involve internal transfers? If yes, which and how many.

Answer: As of September 30, 1981, the Small Business Administration had 4,275 full-time permanent employees on-board. In support of the Administration's efforts to reduce government spending, personnel reductions have been applied across nearly all programs and support areas. When combined with initiatives already underway to increase productivity, these reductions will not significantly impact on our ability to achieve the Agency's mission, and we anticipate no significant delays in providing services to the small business community.

Management Assistance - Through continuing outreach efforts, MA will increasingly rely on the participation of private sector resources. Primary attention in this area will be given to SBA portfolio clients and minority firms. Personnel reductions will reduce the volume of clients that can be served by direct SBA counseling and training, but this shortfall should be offset by increased private sector participation in this effort.

Finance and Investment - With substantial reductions in the guaranteed lending program and the elimination of the direct lending program, it is possible to reduce the loan making staff without negative impact. However, at least part of this staff reduction will be counterbalanced by the increased emphasis and employment required to service the Agency's $18 billion portfolio

Minority Small Business Capital Ownership Development - Reduced personnel levels are possible without detriment to the delivery of program resources. The implementation of new standard operating procedures which streamline program administration, combined with numerous management improvement initiatives, have and will result in smaller staffing requirements for MSB.

Advocacy - Basic Advocacy functions are consistent with the general goals of the Agency and relate directly to the Administration's goals for the Agency and small business. While personnel reduction will not significantly hamper our ability to conform to the standards anticipated by Public Laws 94-305, 95-354, and Executive Order 12138, reduced personnel levels may well be a barrier to maintaining current growth levels in the Advocacy effort. SBA will not relinquish its role as the nation's primary advocate for Small Business.

Personnel Management - The impact of personnel reductions in this area will not retard our ability to provide vital personnel services. The effect will be more slowdown than curtailment or elimination of services, and the slowdown, if any, will likely occur in the institutionalization of basic and entry skills training, and to a lesser extent, in services to operating officials. There can, necessarily, be only minimal restrictions on policy development and guidance.

Data and Management Services - It is expected that personnel reductions can be overcome through increased productivity, streamlining procedures, and reduction or elimination of unnecessary and marginal functions.

Equal Employment Opportunity and Compliance - The Office of Management and Budget has administratively directed that Civil Rights Compliance monitoring, for direct and indirect recipients of financial assistance, not be required for companies with less than 250 employees. This administrative action has not yet officially been submitted in writing. However, we can assume a substantial reduction in workload will occur as a result of this informal mandate.

Field Management - Reduced levels of personnel will be achieved, primarily, through centralizing central office post of duty personnel. Increased productivity will be required to provide direction, oversight, and review to over 100 field offices.

We are not currently planning to reach our reduced employment levels through the RIF process. It is anticipated that with the approval for early out authority and our current restriction on hiring, combined with normal attrition, the Small Business Administration will be able to achieve our new ceilings. As a result of our determination to limit outside hiring, future internal transfers may be necessary in order to properly balance the SBA workload to effectively accomplish the Agency's mission. We fully expect that the majority of transfers will be accomplished as a result of applying for position through the internal announcement process.

ATTACHMENT I

LOAN APPROVALS BY REGION
FY 1981
(Dollars in thousands)

Business Loan Fund	Region I			Region II			Region III			Region IV		
	Allotted	Approval	Balance	Allotted	Approval	Balance	Allotted	Approval	Balance	Allotted	Approval	Balance
7(a) Business Loans												
Direct & IP	11,607	11,487	120	34,852	34,550	302	19,083	18,383	700	27,508	27,508	-
Guaranteed	296,256	189,319	106,937	347,586	237,255	110,331	272,510	197,685	74,825	545,126	406,510	138,616
Total	307,863	200,806	107,057	382,438	271,805	110,633	291,593	216,068	75,525	572,634	434,018	138,616
7(h) Handicapped Loans												
Direct & IP	3,214	3,214	-	2,560	2,558	2	2,368	2,368	-	2,853	2,853	-
Guaranteed	135	135	-	432	432	-	54	54	-	-	-	-
Total	3,349	3,349	-	2,992	2,990	2	2,422	2,422	-	2,853	2,853	-
7(i) Econ. Opportunity Loans												
Direct & IP	3,505	1,836	1,669	10,610	9,758	852	4,820	4,044	776	7,310	6,592	718
Guaranteed	5,209	878	4,331	6,060	3,147	2,913	4,815	2,920	1,895	9,526	2,836	6,690
Total	8,714	2,714	6,000	16,670	12,905	3,765	9,635	6,964	2,671	16,836	9,428	7,408
7(l) Energy Loans												
Direct & IP	295	295	-	1,310	1,290	20	450	450	-	1,018	933	85
Guaranteed	381	370	11	531	530	1	1,005	412	593	3	-	3
Total	676	665	11	1,841	1,820	21	1,455	862	593	1,021	933	88
Development Company Loans												
Direct	1,019	1,019	-	322	322	-	937	937	-	-	-	-
Guaranteed	17,313	7,404	9,909	19,262	5,226	14,036	14,888	5,693	9,195	25,885	5,936	19,949
Total	18,332	8,423	9,909	19,584	5,548	14,036	15,825	6,630	9,195	25,885	5,936	19,949
Total Business Loans												
Direct & IP	19,640	17,851	1,789	49,654	48,478	1,176	27,658	26,182	1,476	38,689	37,886	803
Guaranteed	319,294	198,106	121,188	373,871	246,590	127,281	293,272	206,764	86,508	580,540	415,282	165,258
Total	338,934	215,957	122,977	423,525	295,068	128,457	320,930	232,946	87,984	619,229	453,168	166,061

ATTACHMENT I

LOAN APPROVALS BY REGION
FY 1981
(Dollars in thousands)

Business Loan Fund	Region IX Allotted	Region IX Approval	Region IX Balance	Region X Allotted	Region X Approval	Region X Balance	Agency Wide Allotted	Agency Wide Approval	Agency Wide Balance	Unallotted Balance	Program Level
7(a) Business Loans											
Direct & IP	42,387	38,859	3,528	5,058	5,058	-	214,045	204,931	9,114	4,955	219,000
Guaranteed	406,874	273,640	133,234	189,594	146,094	43,500	3,949,950	2,804,745	1,145,205	50,050	4,000,000
Total	449,261	312,499	136,762	194,652	151,152	43,500	4,163,995	3,009,676	1,154,319	55,005	4,219,000
7(h) Handicapped Loans											
Direct & IP	4,282	4,281	1	1,084	1,084	-	24,988	24,985	3	12	25,000
Guaranteed	64	63	1	50	-	50	1,796	1,713	83	3,204	5,000
Total	4,346	4,344	2	1,134	1,084	50	26,784	26,698	86	3,216	30,000
7(i) Econ. Opportunity Loans											
Direct & IP	12,740	9,747	2,993	1,161	1,133	28	61,631	49,002	12,629	3,369	65,000
Guaranteed	7,170	2,361	4,809	3,290	714	2,576	69,300	20,436	48,864	700	70,000
Total	19,910	12,108	7,802	4,451	1,847	2,604	130,931	69,438	61,493	4,069	135,000
7(l) Energy Loans											
Direct & IP	1,473	1,248	225	235	-	235	7,310	6,723	587	2,690	10,000
Guaranteed	90	90	-	36	36	-	7,864	7,253	611	25,136	33,000
Total	1,563	1,338	225	271	36	235	15,174	13,976	1,198	27,826	43,000
Development Company Loans											
Direct & IP	2,708	2,707	1	-	-	-	5,995	5,993	2	5	6,000
Guaranteed	26,628	23,671	2,957	11,562	2,907	8,655	203,600	66,610	136,990	46,400	250,000
Total	29,336	26,378	2,958	11,562	2,907	8,655	209,595	72,603	136,992	46,405	256,000
Total Business Loans											
Direct & IP	63,590	56,842	6,748	7,538	7,275	263	313,969	291,634	22,335	11,031	325,000
Guaranteed	440,826	299,825	141,001	204,532	149,751	54,781	4,232,510	2,900,757	1,331,753	125,490	4,358,000
Total	504,416	356,667	147,749	212,070	157,026	55,044	4,546,479	3,192,391	1,354,088	136,521	4,683,000

ATTACHMENT I

LOAN APPROVALS BY REGION
FY 1981
(Dollars in thousands)

Business Loan Fund	Region V			Region VI			Region VII			Region VIII		
	Allotted	Approval	Balance	Allotted	Approval	Balance	Allotted	Approval	Balance	Allotted	Approval	Balance
7(a) Business Loans												
Direct & IP	31,568	30,549	1,019	26,969	25,242	1,727	7,048	6,861	187	7,965	6,434	1,531
Guaranteed	762,340	537,022	225,318	549,054	378,674	170,380	331,804	247,683	84,121	248,806	190,863	57,943
Total	793,908	567,571	226,337	576,023	403,916	172,107	338,852	254,544	84,308	256,771	197,297	59,474
7(h) Handicapped Loans												
Direct & IP	3,291	3,291	-	1,730	1,730	-	1,679	1,679	-	1,927	1,927	-
Guaranteed	499	498	1	386	355	31	86	86	-	90	90	-
Total	3,790	3,789	1	2,116	2,085	31	1,765	1,765	-	2,017	2,017	-
7(i) Econ. Opportunity Loans												
Direct & IP	9,140	6,054	3,086	9,700	7,766	1,934	905	760	145	1,740	1,312	428
Guaranteed	13,410	3,495	9,915	9,646	2,066	7,580	5,844	846	4,998	4,330	1,173	3,157
Total	22,550	9,549	13,001	19,346	9,832	9,514	6,749	1,606	5,143	6,070	2,485	3,585
7(l) Energy Loans												
Direct & IP	1,035	1,034	1	233	233	-	75	75	-	1,186	1,165	21
Guaranteed	2,188	2,186	2	545	544	1	878	878	-	2,207	2,207	-
Total	3,223	3,220	3	778	777	1	953	953	-	3,393	3,372	21
Development Company Loans												
Direct & IP	250	249	1	-	-	-	-	-	-	759	759	-
Guaranteed	34,250	8,922	25,328	23,250	681	22,569	17,875	4,975	12,900	12,687	1,195	11,492
Total	34,500	9,171	25,329	23,250	681	22,569	17,875	4,975	12,900	13,446	1,954	11,492
Total Business Loans												
Direct & IP	45,284	41,177	4,107	38,632	34,971	3,661	9,707	9,375	332	13,577	11,597	1,980
Guaranteed	812,687	552,123	260,564	582,881	382,320	200,561	356,487	254,468	102,019	268,120	195,528	72,592
Total	857,971	593,300	264,671	621,513	417,291	204,222	366,194	263,843	102,351	281,697	207,125	74,572

REGIONAL BUSINESS LOAN ALLOTMENTS AND APPROVALS
BY PROGRAM - FISCAL YEAR 1982

($ in thousands)

REGIONS	General Business Direct	General Business Guaranteed	Economic Opportunity Loans Direct	Economic Opportunity Loans Guaranteed	Development Company Loans Guaranteed
I					
Allotted	3,400	68,000	1,300	1,400	9,500
Approved	653	29,650	117	15	3,129
Bal. Rem.	2,747	38,350	1,183	1,385	6,391
II					
Allotted	8,200	161,800	3,100	3,300	9,300
Approved	3,662	26,357	970	44	2,593
Bal. Rem.	4,538	135,443	2,130	3,256	6,707
III					
Allotted	6,000	117,300	2,200	2,400	5,000
Approved	1,865	22,929	148	323	305
Bal. Rem.	4,135	94,371	2,052	2,077	4,695
IV					
Allotted	9,717	181,700	3,400	3,700	7,300
Approved	4,616	56,071	741	225	1,677
Bal. Rem.	5,101	125,629	2,659	3,475	5,623
V					
Allotted	11,800	231,000	4,400	4,700	12,800
Approved	4,127	57,620	773	243	2,523
Bal. Rem.	7,673	173,380	3,627	4,457	10,277
VI					
Allotted	6,800	132,400	2,500	2,700	5,800
Approved	2,181	42,157	541	433	656
Bal. Rem.	4,619	90,243	1,959	2,267	5,144
VII					
Allotted	3,300	64,500	1,200	1,300	6,300
Approved	970	29,503	119	13	1,593
Bal. Rem.	2,330	34,997	1,081	1,287	4,707
VIII					
Allotted	2,000	52,500	800	800	3,400
Approved	616	25,191	179	354	554
Bal. Rem.	1,384	27,309	621	446	2,846
IX					
Allotted	7,000	137,200	2,600	2,800	9,500
Approved	3,227	37,264	790	406	2,055
Bal. Rem.	3,773	99,936	1,810	2,394	7,445
X					
Allotted	2,100	41,000	800	900	3,600
Approved	936	19,663	223	260	613
Bal. Rem.	1,164	21,337	577	640	2,987
SBA TOTAL					
Allotted	60,317	1,187,400	22,300	24,000	72,500
Approved	22,853	346,405	4,601	2,316	15,698
Bal. Rem.	37,464	840,995	17,699	21,684	56,802

Notes:

Bal. Rem. refers to Balance Remaining.

Loan allotment data reflect fiscal year to date as of January 26, 1982. Loan approval data reflect fiscal year to date as of December 31, 1981.

ATTACHMENT II

SMALL BUSINESS ADMINISTRATION
Regional Business Loan Approvals by Program
Fiscal Year 1982
($ in thousands)

Region	Energy Loans		Handicapped Loans	
	Direct	Guaranteed	Direct	Guaranteed
I	65	--	181	196
II	--	--	100	--
III	--	--	300	--
IV	--	--	431	--
V	--	24	138	--
VI	--	45	559	463
VII	--	--	100	--
VIII	--	--	222	--
IX	--	--	478	--
X	--	--	80	--
SBA Total Approved	65	69	2,589	659
Current Program Level	10,000	15,000	15,000	5,000
Balance Available	9,935	14,931	12,411	4,341

NOTE: Loans approved in these categories are allotted on a one-by-one basis, through the Central Office. Loan approval data reflect fiscal year to date as of December 31, 1981.

92-290 O—82——3

RESPONSE TO CONGRESSMAN McDADES'S QUESTIONS
ON THE FISCAL YEAR 1983 CONGRESSIONAL BUDGET

Question #1: The management assistance program appears to offer the opportunity for widest impact on small business. At present, SBA provides at least three forms of management assistance (SBDC, SBI, MAO). It would be helpful to receive a comparative analysis of these three types of assistance, along with your recommendations as to ways in which SBA can improve its management assistance so that it effectively meets the needs of small business.

Answer: The three resources identified should be expanded to include the SCORE and ACE program, which by most measures is the largest of our Management Assistance programs. The cosponsored training program, another very major SBA delivery effort, utilizes approximately two thousand voluntary institutions and organizations to deliver management training should also be included. These efforts, while having much in common, vary significantly in approach, cost, and type of service delivered.

SCORE and ACE - The largest of the Management Assistance "leveraged" resources. The 12,000 volunteers in this program assist in both our counseling and training efforts. The volunteers represent virtually all the management disciplines and offer their expertise and experience to the small business community at very low cost. This resource generally specializes on other than in-depth cases. (The average hours per case is less than 2.0 nationwide.) The volunteers are particularly valuable for problem identification, specific information requests or interviewing. This resource, also completes several thousand in-depth (more than 12 counseling hours) cases each year. The SCORE and ACE resource is also very active in conducting or assisting training sessions each year. SCORE and ACE conducted or assisted in 5,300 training sessions and counseled 131,000 small businesses in FY 1981.

The FY 1983 budget requests $2.12 million for this program to cover travel, clerical support, rents, and operating the National SCORE Office.

SBI Program - Small Business Institute - This program provides in-depth counseling to small business by contracting with colleges and universities on a per client basis. The schools, in return for a fee of $250 per case, provide faculty members and student teams to provide in-depth assistance to the small business client and provide that client and SBA with an oral and written report. An increase in the $250 fee, which has been in effect since 1972, has been

deferred again in favor of retaining a more constant number of businesses helped. In FY 1981 approximately 8,000 counseling cases were conducted with $1.5 million to non-SBDC schools.

SBDC Program - Small Business Development Centers - This program utilizes the resources of colleges and universities to increase the management counseling and training provided to small businesses. Through a cooperative agreement, with the state matching federal funds, the SBDCs provide a wide range of services to the local small business communities using SBDC employees, faculty members, students and a number of leveraged resources. The SBDCs, in FY 1981, conducted 14,200 counseling cases and 1,372 training units.

This program is presently being evaluated with a report due to Congress in January 1983.

Cosponsored Training - One of the most highly leveraged programs in SBA. Cosponsored training was provided to approximately a quarter million people in FY 1981. A very flexible program it also serves as an outreach program for special emphasis.

MAO - Management Assistance Officers - The primary function of MAOs is to manage the many resources and activities that provide management counseling and training to small business. They attempt to locate and develop private sector resources and work closely with the various instititutions and organizations that actually deliver management assistance.

In addition, MAOs provide some management counseling, generally of a problem identification nature designed to match the proper assistance delivery resource with the troubled small business. They do some counseling, generally when an adequate resource is not reasonably available.

SBA will continue to develop private sector resources to assure that small business has access to the specialized expertise they need at reasonable cost to the government. Our efforts will stress the continuing growth of private sector participation and the careful management and coordination of those resources.

We will continue our program of identifying and upgrading the quality of SCORE and ACE skills, increasing small business training activities available through the AACJC and other colleges, and significantly increase our search for private sector resources willing to cooperate with our efforts to assist small business.

QUESTION 2: This Administration has placed great emphasis on the reduction of waste, fraud and abuse through the operations of the Inspector General. Indeed, the budget proposal calls for an increase in the SBA Inspector General's budget. However, there has not been a thorough analysis of the Inspector General's performance. What standard would you recommend as the most accurate measurement of the Inspector General's performance? In particular, how would you recommend that the performance of the Inspector General in monitoring SBA's loan processing performance be evaluated? Finally, I would appreciate your advising the Committee as to SBA's policy for providing access to documents relating to Inspector General investigations (including inspection reports) by Committee members.

ANSWER: You raise three issues in this question.

(a) "There has not been a thorough analysis of the IG's performance. What standard would you recommend as the most accurate measurement of the IG's performance?

Ongoing review and oversight is provided by OMB through the IG's active involvement in the President's Council on Integrity and Efficiency.

GAO has from time to time evaluated the OIG with not significant deficiencies noted. Furthermore, the IG is required to comply with the CG standards for audits.

Most significantly, and in furtherance of the IG Act, the Inspector General transmits Semi-Annual Reports to all Congressional Oversight Committees in May and November of each year. A review of these reports provides Congress with a measure of the effectiveness of the IG and was one of the tools Congress believed was essential to their monitoring of the IG's. I would note that the most recent Semi-Annual Report observed that for a six month period, the OIG recovered $6.7 million in cash and reduced the risk associated with another $37 million.

(b) "How would you recommend that the performance of the IG in monitoring SBA's loan processing be evaluated?"

Monitoring the effectiveness of our loan processing (and other activities) is the primary responsibility of program managers as is aggressive follow-up on audit findings. The Associate Deputy Administrator is responsible to the Administrator and OMB for this function.

The OIG is presently conducting a survey of loan processing the results of which would be available within the next 60-90 days. To the extent that these findings disclose areas for management improvement or suggest more effective ways to conduct our loan processing activities, they will be used by program managers to enhance their efforts in this area.

Once program officials have agreed to take action, the OIG will follow-up on a periodic basis to ensure that agreed upon action has been taken and that it has been effective in resolving issues raised by the OIG.

(c) "I would appreciate your advising the Committee as to SBA's policy for providing access to documents relating to IG investigations (including inspection reports) by Committee members."

Must differentiate between documents relating to IG investigations but not created by the OIG (e.g., underlying loan/contract files), and documents created by OIG in conduct of its investigative activities. In the former situation, Agency policy is governed by Section 10(e) of the Small Business Act and other statutes governing the privacy and release of documents. The current policy is under review in light of a recent decision in Murphy vs Dept. of Army which stated that the release of exempt information should not be limited to Committee Chairpersons. When our review of the impact of this decision is completed, we will be happy to inform you.

In the latter case, Agency practice in regards to requests for access by Members of Congress to IG investigative records has been devised in consultation with the OIG. Basically, all such requests are referred

in this instance, to the OIG. Consistent with current FOIA law, investigative records (like Agency records) are generally made available by the OIG to Members of Congress acting other than as Chairman of Committee or Subcommittee and are processed in accordance with procedures applied to requests generally.

As with such requests, and especially in connection with open cases, particular care is given to assure proper handling of often sensitive investigative information as to methods, sources, and similar protected data.

Question #3: In recent years, the Appropriations Committee has earmarked funds for improvement of SBA's computer operations. However, serious problems remain in your computer capability. What are the obstacles that have prevented SBA from obtaining an adequate computer capacity? Whay do you plan to do to resolve this problem?

Answer: The Small Business Administration has had problems with increased production demands combined with a constant change in top management's directions and priorities pertaining to data management. Another obstacle has been the replacement of antiquated peripheral (Tape/disk) equipment. During FY 1980 we replaced our computer with a UNIVAC 1100/81 but did not have adequate funds to replace the peripheral equipment. This antiquated equipment has been the major cause of computer downtime resulting in constant rerunning of computer jobs and inefficient use of computer resources. This problem will be resolved within 90-120 days. Also, another problem has been the design of many of the major processing systems. We are currently redesigning our major systems using modern technology (data base management system). The initial effort in this area is scheduled for completion within 6 months. The actual redesign/rewrite of the system is scheduled to begin in June 1982 and, due to the magnitude of the effort, will continue into FY 1984 before completion.

Some of the significant improvements, by fiscal year, are as follows:

FY 1979

Completed ADP and Communications Planning Project

Expand Time Sharing Service to provide quick response to users

FY 1980

Installed new computer system (1100/81)

Installed nationwide network

Implemented training program to increase productivity

Trained all field locations on operation of network equipment

Reduced backlog of User Requests (for ADP service)

Implemented Loan Tracking System for Field Offices

FY 1981

Installed Message Transmission System to increase the speed of communications to and from field offices

Improved Application Tracking System (on-line)

Published Long Range (Five Year) Plan

Purchased Network Equipment to save $

Received OMB/GSA approval to retain 1100/81, purchased 1100/81 (lease - purchase agreement)

Installed new 8(a) Financial Information System (on-line)

Published and tested plans for off-site operation during emergency conditions (severe or prolonged computer outage).

FY 1982 Planned

Procure and Install new Peripheral Equipment (Disk/Tape)

Implement Charge Back System (OMB A-121)

Convert Loan Accounting/Loan Collection to a single data bas

Absorbed large increase in communications cost (AT&T)

FY 1983 Requested

Rewrite major systems

Improve service to Portfolio Management function

Reduce backlog of User Requests

Extend terminal service to additional field offices

The following chart reflects the cost of operation subdivided by major category.

	FY 1979	FY 1980	FY 1981	FY 1982 To Date
Rent and Maintenance:				
ADP	$510,512	$1,340,981	$1,443,832	$1,952,783
Telecommunications	172,751	878,684	1,390,823	1,191,827
Total	$683,263	$2,219,665 (1)	$2,834,655	$3,144,610 (2)

Other Contractual Services:

Software support	$408,640	$137,906	$223,251	$257,193
8(a) FIS	760,000		77,351	
Programming 8(a) engineering	259,500			
Keypunching	25,600	264,000	241,000	
Programming Support		615,939	724,501	641,040
Network - (SBADCS)		2,121,703 (3)	1,891,167	-
Network - Maintenance				387,000 (4)
Total	1,453,740	3,139,548	3,157,270	1,285,233
Total (million)	5.1	8.7	10.9	11.3

(1) Univac 1100/81 Computer procured.
(2) Procurement of new disk/tape equipment.
(3) SBA Data Communications Network implementation.
(4) Equipment purchased and Network maintenance contracted with a different company at reduced cost.

Question #4: Another emphasis of this Administration is improved portfolio management. SBA is straddled with a large number of delinquent and defaulted loans. How do you plan to allocate resources to improve your debt collection performance, as well as assist small business owners to work their way out of their current delinquencies?

Answer: The Small Business Administration has allocated for FY 1983 a total of 863 positions for servicing the portfolio. District office by district office determinations being made where large portfolios combined with extensive problems exist to subdivide the Portfolio Management unit into a "servicing" section and a "liquidation" section. Currently, we can estimate that 275 of the 863 positions in the field are occupied by "liquidators." In conjunction with the intensified efforts of liquidators, these district offices are assigning a lawyer (counsel) of the district staff to work exclusively with the liquidation cases. Where a mutual agreement can be reached with U.S. Attorneys, a designation of Special Assistant U.S. Attorney is being sought to allow much greater ability of SBA to pursue legal remedies. As of September 30, 1981, SBA had twelve such designations. We intend to increase that to twenty-four by September 30, 1982. Approximately two dozen individual efforts between counsels and U. S. Attorneys are now in process.

Significant improvement in computer/communications is well on schedule. Funds have been authorized and virtually spent to significantly update software in our Univac so that collection data provided to field offices is accurate and timely. Hard copies of loan data on 500,000 loans which is routinely six weeks old when it gets to the field offices by U. S. mail will be replaced by electronic data transfers on T.V. screens and through high speed printers now installed in all offices except Puerto Rico, Alaska, and Hawaii.

Over 76% of our borrowers are meeting their payment obligations to the SBA (and banks guaranteed by SBA) on current basis. The other 24% - about 125,000 borrowers which include disaster home loans, farm loans, and business loans are and will continue to be dealt with on a case by case basis. We can defer (delay) payments for three or six months if there is good reason to conclude that such a delay will result in a "cash flow" turnaround. We can continue to allow borrowers who are one or two payments behind to remain delinquent but who anticipate catch-up payments in the near future. We can rewrite the note if absolutely necessary to extend the terms and thereby reduce monthly payments. The penalties for delays or deferments result from the fact that interest due on

the outstanding principal balance continues to accrue. While direct loan interest rates are low when compared to current market rates, SBA borrowers in these distressed conditions do have a motivation to bring their loans current.

We will treat borrowers who want to pay but can't with every reasonable tool at our disposal. For those who can pay and won't, we will pursue collections with appropriate methods at our disposal.

While pressing for regular payments in accordance with the basic loan agreement, we realize that unforseen difficulties do arise, and that the best recovery for the Agency results when the borrower's viability is maintained. We are, therefore, "work-out" oriented and do allow reasonable latitude to bring about successful repayments in full. Remedial relief as described above - deferments, delays, refinancings - are utilized in varying degrees.

Faced with liquidation type circumstances, we rely primarily on business assets for recovery. To the maximum extent possible, we utilize the authority available under the Claims Collection Act of 1966 to compromise and settle with borrowers for amounts that are reasonably comparable to the amount we could expect in enforced collection actions such as suits, foreclosures and judgments.

Mr. MITCHELL. Thank you very much.

In the ranks of a reducing number of people and entities that support the administration's program, I noted with interest that some of the small business trade associations now are raising serious questions about the effectiveness of the program that you are locked in. Twice in your testimony you indicate you want the Small Business Administration to continue to be an advocate for small business. That was in the first part and in the closing portion.

Mr. TEMPLEMAN. Yes, sir.

Mr. MITCHELL. Yet in your budget I see that you have significantly reduced funding for the Office of Advocacy. Congressman Ireland, who is not here with us, has discussed this with me privately. He is concerned about the reduction in the work of that office, the Office of Advocacy. I don't see how you could approve a cut there and yet at the same time insist that you want to be the advocate for small business.

Mr. TEMPLEMAN. We believe, if you're ready for me to respond——

Mr. MITCHELL. Sure.

Mr. TEMPLEMAN. We believe that the reduction of personnel in Advocacy, which is, of course, like the reduction in personnel in the rest of the Agency, is manageable. The Agency is staffed with essentially temporary people in terms of public law employees in that portion of the Agency. Frankly, it appeared to us a year ago, approximately, when we came there, that there were more than were required.

One of the major functions of that office is the database that is being developed on small business, a very important thing, no doubt. It will continue. The major functions of that office will proceed, even though there is a significant reduction in dollars and personnel.

Mr. MITCHELL. You personally approved the reduction in funding for that office?

Mr. TEMPLEMAN. Well, that was before I was the Acting Administrator.

Mr. MITCHELL. Oh, yes. That's right. I'm sorry.

There is a reduction of personnel of 170 people, is that correct? What's the number of persons?

Mr. WRIGHT. Those are permanent reductions.

Mr. MITCHELL. I'm talking about overall in your budget.

Mr. TEMPLEMAN. It's 220.

Mr. MITCHELL. All right, 220 people.

How in the name of God can you justify a personnel reduction like that, when you have complained about the inability of the Agency to handle the loan programs properly—and I understand why you complained. You've got people sitting over there with a portfolio of 500 loans for every 1 person. Of course, you're not going to stay on top of your loan program. No lending institution in the world would maintain that kind of completely disproportionate ratio of loan officers to volume of loans.

How can you square that kind of reduction with the problem that you and others from SBA have come in to talk to us about time and time again?

Mr. TEMPLEMAN. We believe we can adequately operate with reduced funding by doing some other things. One of the things that has grown up in SBA over the years is the total inadequate allocation of resources among programs and among regions. We are looking at that entire thing.

There are places in SBA where there are too many people. There are places, more places, where there are not enough people to do things as they are currently done. For instance, I know you're personally familiar with the district office problem in Washington. We are moving more people in there, even though next year that program will be reduced in total number of people.

Part of the efficiencies will come by a better allocation of people. Part of the efficiencies that will allow us to do this will come from changing our emphasis: for instance, in the management assistance area, from trying to do direct counseling with a very limited number of people, to having even fewer people do coordination of other people that do direct counseling.

Mr. MITCHELL. Forgive me. I guess I am disadvantaged. I just don't understand that kind of thinking at all.

In 1981 you allowed more than $33 million to lapse in direct loan money. In the first quarter of this year you approved $31 million of the $56 million available. Why did you allow that money to lapse?

Mr. TEMPLEMAN. The problem in the latter part of 1981 was that we had been allocating funds based on a reduced level up until the last quarter. I have forgotten the exact documents they used, but we finally got our budget. We increased $43 million in the last quarter over what we had allocated originally. That, plus the increase in interest rates that went up to the cost of Treasury plus up to one, made the demand not as significant as it had been. The demand was not great enough to take up that slack. We simply didn't have time to get the money loaned for the most part.

[The information referred to above follows:]

U.S. SMALL BUSINESS ADMINISTRATION,
Washington, D.C., August 27, 1981.

To: All Regional Administrators; District Directors; and Branch Managers.
From: OBL/Hertzberg.
Subject: Direct Loan Funds.

A recent survey has indicated a considerable amount of direct funds available in some regions which will not be used by fiscal year end.

As you all know, specific numerical targets were abolished for this fiscal year.

While the priority group use of direct funds is still emphasized, it is not considered appropriate to withhold those funds from non-priority group applicants in the absence of creditworthy priority applicants with only five weeks remaining in the fiscal year.

Further, based on field office information, the Central Office has consistently advised prospective applicants, Members of Congress, and other interested persons that funds are short, waiting lists are long, and prospects for obtaining direct loans are slim. Under these conditions, it would be difficult to justify returning a substantial amount of unused loan funds.

Those offices that have creditworthy applications that justify approval should use available direct loan funds to approve them regardless of priority group allocations.

Offices that lack a supply of creditworthy applications and, as a result, could have unused direct funds at the end of the fiscal year are asked to notify Larry Rosenbaum (FTS 653-6347). At the same time, those offices that have more creditworthy applications than available direct funds will cover are also asked to contact Larry

Rosenbaum. The Central Office will, to the extent possible, match the available funds with the creditworthy applications awaiting funding.

EDWIN T. HOLLOWAY,
Acting Associate Administrator
for Financial Assistance.

Mr. MITCHELL. That was an unusual circumstance last year. But in past years you had no difficulty in using the entire amount of your direct loans. In your own testimony you indicated that SBA has always had the problem of allocation of scarce direct loan resources among competing interests; is that not true?

Mr. TEMPLEMAN. That is true. However, the fact that we got caught in the last quarter, and to be quite honest about it, some rather restrictive policies by the former Administrator on not so much in actually restricting loans but improving quality, combined with the increase in the interest rate, it was not possible to get that money out there.

Mr. MITCHELL. All right.

I am utterly, bitterly, completely opposed to the elimination of direct loan money. It is very, very clear to me that whoever made this policy decision simply does not know what's going on out there in the world. Except for MESBIC's, you propose to eliminate all direct loan money. You say then people can go to the banks or to the MESBIC and get the money they need.

Well, that is simply not true, Mr. Templeman. We had testimony in field hearings around this country, four different cities. In every instance there was more than adequate testimony to show the reluctance on the part of the banks, save for one or two major exceptions, the reluctance to make these guaranteed loans. That reluctance was compounded by some of the uncertainties that were surfaced by the former Administrator such as reducing the amount of the guarantee to 50 percent and all that kind of foolishness. Those loans have not been made.

Where are the people going to go if you cut out the direct loan money? No matter what you're pushing to MESBIC's, that is not going to be sufficient to meet the need. I would hope that the members of this committee would join me in preventing this kind of unilateral policy decision which does not take into account the real world. The banks are cautious; they have been made even more cautious because of the fuzzy policy statements that were emanating from SBA last year. Banks traditionally are unwilling to lend to minorities, primarily because these are high-risk loans. We take that into account. Mr. Addabbo alluded to the fact that is precisely why we put the direct loan money in there in the beginning.

Quite frankly, I feel that, honestly, this is just an—let me see if I can use the right word—this is an attempt to end the agency. I would be much more comfortable if we had a situation like with the Department of Education, where somebody simply comes out and says "We're going to end it." That's being honest and fair and square. But instead, to do it this way, by cutting away at funding, by putting out the most insane kind of regulations, by doing things that will obviously prevent the agency from operating and that will erode any confidence in it, you will have destroyed it.

I am sorry if I am worked up about this, but I think we made a commitment as a Congress to the small business community, and I

see this budget as an absolute reneging on their commitment, no matter what words you use in your testimony to make is sound more palatable.

Mr. Addabbo, you are recognized.

Mr. ADDABBO. Thank you very much, Mr. Chairman. I fully agree with you. You know, you're a good soldier, Mr. Administrator, and I commend you for it. I hope I'm not reading what's in your heart but reading what has been cleared by OMB.

Do you know if SBA received any instructions from OMB, officially or unofficially, to actually slow down, withhold, or otherwise avoid making the necessary or requested direct loans?

Mr. TEMPLEMAN. No, sir, we have not.

Mr. ADDABBO. The chairman had posed a question relative to the amounts used up in your direct loan program, and your answer to the chairman was that these funds were not extended but somehow the demand for direct loans had actually or possibly subsided. Could you state for the record now how many actual loan applications were made and how many were granted?

Mr. TEMPLEMAN. I would like to ask Mr. Holloway to give you more details on that, if he can, at this point.

Mr. ADDABBO. All right.

Mr. HOLLOWAY. I do not have those specific figures with me, Congressman. However, I can state for you that, both in the guarantee program and the direct program, demand is off. Demand is off in the SBA business; demand is off at banks in non-SBA business.

Mr. ADDABBO. I can understand the demand being off from banks, which have higher interest rates. I'm talking about direct loans.

How many applications were made? I don't care if you had 50,000 last year, and 40,000 this year. If you only had 40,000—— What is the total of that 40,000? Didn't those 40,000 applications account for requests for more than $47.5 million that you had on hand?

Mr. HOLLOWAY. Congressman, I do not have those specific figures before me.

Mr. ADDABBO. I wish you would supply them for the record.

Mr. HOLLOWAY. Yes, sir, I would be glad to.

Mr. ADDABBO. I mean, you had $47.5 million on hand. I am willing to wager that you had more requests for more than that $47.5 million by applications. I am wondering whether all those applications that were put in, whether by the end of the fiscal year they were actually processed.

Mr. HOLLOWAY. As of August, our interest rates on direct loans, by changing the law, went to roughly the cost of money to the Government, so those loans are now at around 15¼ percent at the present time, which puts them more near a market rate and also is a factor in demand.

Mr. ADDABBO. I understand that, which would give some reason for the falling off of the applications. But I am still wondering whether you had more applications than you processed and whether those applicants were even willing to pay the 15-plus percent in order to get a direct loan and they just were slowed down, just put aside so they would be discouraged, that you would discourage and completely denigrate the direct loan program.

Mr. HOLLOWAY. Congressman, we are not discouraging those applications, nor are we discouraging the program. As a matter of fact, just recently we went out with instructions to our field offices along the lines that any field office that is running short of money in direct programs, guarantee programs, come in to us and we'll switch money around to make a good faith effort to use the direct money that has been provided.

Mr. ADDABBO. Well, again, supply for the record the breakdown on the number of applications and how many were granted and how many were not granted, how many were still pending.

[The information requested above follows:]

For the period October 1, 1981 through January 31, 1982 the agency approved 737 direct and I.P. loans for $37.8 million. On January 31, 1982, there were 126 direct and I.P. loans pending for $10.1 million.

These figures were obtained from our management information summary. At the present time our system does not tell us the number of declined applications nor does it tell us the number of applicants on so-called waiting lists around the country.

In order to eliminate the possibility that otherwise eligible direct loan applicants would be denied access to funds in one part of the country while funds remained unused in another, we have recently contacted all field offices to urge that they request needed funds so a redistribution may be accomplished.

Mr. ADDABBO. In my opening statement I alluded to the question of personnel. We know there are a number of vacant positions at the present time. Do you have the total number of vacant positions now? Can you supply them for the record?

Mr. TEMPLEMAN. We can supply it for the record.

[The information requested follows:]

SMALL BUSINESS ADMINISTRATION—PERSONNEL

[Analysis by activity]

	1981		1982		1983	
	Authorized	End of year	Authorized	End of year	Authorized	End of year
Procurement assistance	213	194	194	188	188	183
Management assistance	408	381	381	285	285	280
Finance and investment	1,806	1,565	1,565	1,556	1,556	1,400
Minority small business COD	367	370	370	361	361	327
General counsel	378	347	347	343	343	337
Policy, planning and budgeting	194	172	172	158	158	158
Advocacy	46	47	47	35	35	35
External affairs	43	42	42	38	38	38
Personnel management	49	44	44	40	40	40
Data and management services	201	175	175	162	162	162
Equal employment opportunity and compliance	45	47	47	30	30	30
Inspector general	144	130	130	130	130	130
International trade	8	8	8	17	17	17
Field management	33	32	32	23	23	23
Field administration	361	444	444	399	399	385
Executive direction	262	277	277	271	271	271
Total	4,558	4,275	4,275	4,036	4,036	3,816

Based on the original 1982 ceiling there would presently be 35 vacancies. However with the revised ceiling at 4,036 there technically are no vacancies. There are presently 9 SES positions vacant within the 53 positions authorized to the Agency.

They are as follows: 1. General Counsel; 2. Director of Field Management; 3. Deputy Associate Administrator for Finance and Investment; 4. Deputy Associate Administrator for Financial Assistance; 5. Deputy Associate Administrator for In-

vestment; 6. Deputy Assistant Administrator for Policy, Planning and Budgeting; 7. Director of Business Development; 8. Deputy Regional Administrator—Seattle; and 9. Deputy Regional Administrator—San Francisco.

The 35 vacancies are as follows:

Schedule C's	2
Senior executive service	9
Field positions (GS–13 to GS–15)	24
Central office	0
Total	35

The 24 field positions are as follows:

District directors	11
Deputy regional administrator	1
Assistant regional administrators	6
Deputy district director	1
Assistant district director	1
Branch manager	1
Regional counsel	1
Procurement assistance positions	2
Total	24

Mr. TEMPLEMAN. I would like to make one comment in regard to that. There are vacant positions, not a great number, I don't believe, relative to the total. We have been slow to fill some of them, knowing that we are faced with reductions in personnel. We need to have some latitude. Also, it doesn't make a whole lot of sense to hire people with the expectation that they're going to have a job for some period of time and then find out they don't. So we admittedly have been trying to let attrition take care of our need to reduce our total personnel.

Mr. ADDABBO. I can understand, that when the word gets out that the administration is trying to do away with the Small Business Administration, nobody would want to take that job. We have an Acting Associate Administrator who is very qualified, Mr. Holloway, Acting Associate Administrator for Finance and Investment. But this position has been "acting" for quite a long period of time. Why wouldn't that have been a permanent position?

Mr. TEMPLEMAN. As of yesterday Mr. Holloway is the Associate Administrator.

Mr. ADDABBO. Now we can pin it all on him. OK.

Mr. TEMPLEMAN. He's now your man.

Mr. ADDABBO. I am happy to see they finally, after 15 months, have gotten some sense. I am happy also that some of the personnel they are putting aboard have some expertise as far as SBA is concerned.

In attachment II of your testimony you indicate that no energy loans, either direct or guaranteed, were approved in region II. That just happens to include New York State.

How many applications were actually made in that region, if any?

Mr. HOLLOWAY. Congressman, I do not have that material, but I will be glad to submit it for the record.

[The information follows:]

In this fiscal year we have not received any energy applications from region II.

Mr. ADDABBO. Thank you.

Your testimony emphasizes SBA's role in the areas other than financial assistance, such as procurement assistance, and you state the SBA will "continue its efforts to assure that small business receives its fair share of Government procurement;" that SBA has negotiated procurement goals with agencies amounting to $3 to $3.5 billion more than last year.

Now, that seems very admirable. I think it probably could be twice that amount, but that is admirable if you look at the dollar figures. But then when we look at the percentage figures, we find this percentage goal is approximately 17.6 percent. Then when we look at 1981, we find the actual accomplishment for procurement was about 18.9 percent. In other words, you're setting a lower percentage goal with a higher budget; you're setting a goal less than the actual 1981 accomplishment. Why is it a reduction rather than increase?

Mr. TEMPLEMAN. The reason that the total is lower is the difference in the so-called procurement mix. We are now moving away from procurements in the civilian agencies toward DOD. While DOD does a fairly good job in small business, a great many of the dollars in DOD go for major weapon systems. The subcontracting area picks up on small business.

Mr. ADDABBO. That's what DOD tells me. But I tell them that under the rules the small businessman cannot make a maverick. He could probably make a maverick better than the big business guy——

Mr. TEMPLEMAN. I would agree with that.

Mr. ADDABBO. Who is working on it now. But if they broke out parts of those large systems and did their job according to 95–507, and really did a job rather than just trying to fulfill the letter of the law, not by giving out a service contract, a cleaning contract, janitorial services, but go out and do some work in those major contracts, we say you can get competition because you will find out there are one or two or three small businessmen who would be willing to compete. So don't try and apologize for DOD. I know they're going to give you a rough time.

I had Weinberger before me for 2 days and I told him the same thing. I told him I sit with two hats. If I don't catch you with one, I'll catch you with the second one.

Mr. TEMPLEMAN. Congressman, you will not find me apologizing for——

Mr. ADDABBO. You've got to push them.

Mr. TEMPLEMAN. We do.

Mr. ADDABBO. You can do it, Templeman, I know you can.

Mr. TEMPLEMAN. We are pushing harder. You mentioned breakouts. In terms of breakouts on spare parts, which are a major source, a fertile ground for small business, we are moving into a program that we call the spare parts breakout program. This means that breakout PCR's go in and look at spare parts formerly purchased from a major supplier, actually get the data and find—quite frequently—they are a small business part with somebody else's part number on it. We have made great strides within the last few months with only four of those people. We are now looking, even with these limited personnel figures, we are looking at

restructuring some of our PCR's to get qualified people in to do that.

I agree with you 100 percent. The breakout is how we have to go, and we have to push DOD harder. That is one of the things we can do.

Mr. ADDABBO. I think it is very important. You bring up a very good point on spare parts, because my subcommittee pushed all the money into that program, because our readiness was deteriorating due to the failure of spare parts, because we relied on the big businessman to supply it. Now we're getting the breakout and getting the spare parts into the system.

Also, which we proved to the Secretary of Defense, we had one corporation that was supplying the spare part to the Government at $190,000 for the part. He paid the small businessman $9,000 to make that part. So we go direct, and will be able to save all that money——

Mr. TEMPLEMAN. Absolutely.

Mr. ADDABBO. And use it for other small business.

The other thing that concerns me—and I want to make this a part of the record—as we look at the analysis by activity of the personnel within the Small Business Administration, we see a continuing deterioration. We see in 1981 procurement assistance, for argument's sake, authorized at 213 and you ended up with 194. You then start 1982 at the authorized level, the end-of-year level, at 194, and you end up with 188. Then you go to 1983 and you take that low figure of 188 and then go down from there. In every one of the activities we see the same thing. So if you spell this out, we all of a sudden get down to 1985 and 1986 with zero at the end and zero into the succeeding year.

Mr. TEMPLEMAN. Obviously they are diminishing numbers. I don't honestly believe it is to remove the agency. We took the same percentage cut from OMB that all the other civilian agencies did, except possibly one or two.

In my negotiations with OMB on this and other matters, I would share with you that some of the cuts originally were intended to be higher than that.

Mr. ADDABBO. What we have also seen is that you have taken the cuts which OMB supposedly has equalized among all the agencies. Then internal pressures cause positions to remain unfilled by the end of the year, even though you were authorized for it, as we see here. OMB then takes that as your final figure on to the next year and then gives you a lower figure off that. So I think we have to fight OMB, and I will join with the Chairman to make sure we get the proper personnel levels and make sure they are properly funded, and then we'll make sure that OMB makes you spend the money for it.

Thank you, Mr. Chairman.

Mr. MITCHELL. Thank you, Mr. Addabbo.

Would the members indulge me for just one quick question? Mr. Weber is next.

I have a problem. The Joint Economic Committee is having a meeting also and I want to get this one comment in and then I might slip down there for a minute.

What concerns me is that next week, I think, the President's Report on Small Business and Competition will be released——

Mr. TEMPLEMAN. Monday, I believe.

Mr. MITCHELL. Monday; and that report will show that the small business community is getting a much smaller portion of Government guaranteed loans than any other sector of the economy—any other sector.

Just by way of illustration, we recently guaranteed $1.4 billion to the synfuels project, $1.4 billion, and that amounts to one-half of the 7(a) guaranteed loans for all small business for the year. There is something wrong with our priorities in this Government for small business if that kind of thing takes place.

Dwell on it a little bit and maybe later on you can respond to me.

Mr. Weber?

Mr. WEBER. Thank you, Mr. Chairman.

Mr. Templeman, the chairman has stated his belief that the removal of the direct loan program from SBA is essentially the first step toward eliminating the agency, that you might as well just quit business.

I notice on page 5 of your testimony you point out that under the guaranteed loan program for 1983 you will be allocating 17 percent, or approximately $410 million, for firms that are owned by socially and economically disadvantaged individuals, as compared with an average over the past 5 years of 9 percent minority participation in the guaranteed loan program, and 12.8 percent minority participation overall. I have two questions along that line.

First of all, how does the dollar amount of $410 million compare with the dollar amount averaged over the last 5 years? I recognize that 17 percent is an increase in percentages, but if the overall amount available goes down, what is the effect on the dollar amount?

Mr. TEMPLEMAN. In 1981, the dollar amount was approximately $410[1] million, combining direct and guaranteed loans for minorities. It was $147 million in direct and the remainder in guarantees. So the dollar amount that is being reserved, if you will, is the same as was experienced in 1981. The percentage goes up because the total, of course, is smaller.

Mr. WEBER. And do you have a projection on how that would compare with what you're expecting to do in fiscal year 1982?

Mr. TEMPLEMAN. I'm sorry, I don't quite understand your——

Mr. WEBER. How would the $410 million compare with what you're expecting for fiscal year 1982? You mentioned 1981, didn't you?

Mr. TEMPLEMAN. Yes. This goes back to the 1981 base. In 1982, it would be about the same.

Mr. WEBER. About the same. So the $410 million, if you looked at both the direct and guaranteed loan programs, would be relatively the same, at least no decrease?

Mr. TEMPLEMAN. That's right.

Mr. WEBER. Will there be sufficient qualified applicants for that $410 million?

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[1] Corrected for the record to $414 million.

Mr. TEMPLEMAN. We don't know. Of course, they are based on a combination of guaranteed and direct. With the economic conditions being what they are, I'm not sure. We will do a promotional effort with the banks and try to overcome some of their reluctance and promote the fact that we're interested in using the guaranteed program for minority and disadvantaged companies.

There is no way at this point in time to predict whether that direct loans will fully convert to guaranteed, although we believe many of them will.

Mr. WEBER. My last question: If 220 employees are to be eliminated, how many employees will that leave in the agency?

Mr. TEMPLEMAN. At the end of 1983 it will be 3,816.

Mr. WEBER. So you will still have 3,816 employees?

Mr. TEMPLEMAN. Yes.

Mr. WEBER. Thank you very much. I will turn back the balance of my time.

Mr. ADDABBO [presiding]. The gentleman from Indiana, Mr. Hiler.

Mr. HILER. Thank you, Mr. Chairman.

I would just like to dwell on the direct loan area here, because I think that is probably going to be the most controversial area. How many direct loans were made last year?

Mr. TEMPLEMAN. 5,400.

Mr. HILER. How many guaranteed loans were made last year?

Mr. TEMPLEMAN. Roughly 23,000.

Mr. HILER. What is the approximate number of small businesses in the country?

Mr. TEMPLEMAN. 13 million.

Mr. HILER. How much time is devoted to making those 5,400 direct loans? You have 4,000 man-years last year——

Mr. TEMPLEMAN. I think Mr. Holloway could give you a better idea of that.

Mr. HOLLOWAY. Probably you could say about 1 to 3 man-days of processing time per direct loan. That would be a good estimate.

Mr. HILER. That's 5,400 man-days. Does anybody have a calculator around here? What was the default rate on those 5,400?

Mr. HOLLOWAY. The actual loss rate I believe was about 8.4 percent, cumulative.

Mr. HILER. I would like to enter for the record a series of articles that appeared in the St. Louis Globe-Democrat.

Mr. ADDABBO. In the Globe-Democrat? Without objection. [Laughter.]

[Articles referred to above follow:]

[From the St. Louis Globe-Democrat, Aug. 31, 1981]

MILLIONS LOST IN SBA LOANS: 42 PERCENT OF BORROWERS END UP IN DEFAULT AND OUT OF BUSINESS

(By Thomas L. Amberg and Michael R. Montgomery)

More than $571 million in taxpayers' dollars has been lost as more than two of every five loans have ended in default in the Federal Government's primary program to help the underprivileged enter the mainstream of American business.

Rather than help the disadvantaged, as the program was designed to do, recipients often become its victims. The program often ends up putting people out of

work, draining life savings and creating intense frustrations while leaving a trail of closed shops and broken lives, hundreds of interviews have revealed.

The high failure rate results in part from a pattern of making significantly smaller loans to borrowers in minority urban areas than elsewhere, and a history of giving loans to totally unqualified people.

After a long, intensive nationwide investigation, The Globe-Democrat found that lax policies and sloppy procedures in the Small Business Administration's direct business loan program from 1970 through 1978 have cost the Federal Treasury $571,228,200—a figure that could reach $900 million if losses in 1979 and 1980 are consistent with previous years.

Across the country, many SBA officials interviewed said the program should either be scrapped or completely overhauled. The officials interviewed agreed the program has serious problems.

Loan recipients whose businesses failed were more outspoken. "I wish they'd never lent me the money; I'd have been better off," said one man. His comment was repeated time and time again by other borrowers across the nation.

"It's as if the money were soap and we're supposed to peddle it," said Bernard Lump, a chief liquidation officer. "It's a fact. There is no respect for money in this agency. I'm appalled at this stuff. We're not helping these people."

That feeling was echoed by Clyde Cromwell, an official in the Dallas district office. "I've gone back to a loan officer on occasion and said, 'What in heaven's name are you doing making this loan?' and he's said, 'Got to get the money out, man. You get no brownie points for declining a loan.'"

Added Denver District Director Chester B. Leedom, "We don't do a man any favors by putting him in business with an artificially low interest rate and without proper management ability."

In fact, the actual default rate within the program is masked by a widespread policy of granting deferments to loan recipients who have missed payments, artificially understanding losses. The purpose in granting the deferments is often to make a loan officer or a district field office "look good," SBA insiders said.

Lump, who has served in SBA offices in New York, Los Angeles and now San Francisco, said, "I would say that, at any time, 10 to 25 percent of the direct loan portfolio would be in deferment status, which means we just stopped collecting money on those loans."

Lump explained that by deferring loan payments, loan officers are able to transfer the loan from a delinquent status to a "current" status, thus making their portfolio appear to contain a greater percentage of good loans. That can mean more money and faster promotions for the loan officers because the agency has had an incentive program targeted largely on such things as high percentages of current loans, he said.

"I was part of the 'we' that did it," Lump declared. "I know. We were the No. 1 office in New York, and when I was in LA it was the same, but it was all a charade. It's just a way to hide the actual default and delinquency rates. People do it to protect themselves and get ahead."

When The Globe-Democrat informed SBA Administrator Michael Cardenas that it had found a 42 percent default rate, Cardenas expressed no surprise, admitting that the program has been poorly handled for years. He said he intends to change the direction of the program but offered no specifics.

Asked what he felt was an ideal or reasonable default rate, he replied, "I'd like to see it no higher than 10 percent."

The direct loan program, set up in 1953, was expanded in 1964 and again in 1969 as a response to urban riots in the late 1960s. While there are several types of direct loans, the overall purpose is to enable marginally qualified borrowers to enter the free enterprise system by owning and operating their own businesses. The threshold requirement for receiving an SBA direct loan is to be turned down for the loan by at least two banks and not to qualify for even a 90-percent SBA-guaranteed loan.

The SBA generally requires a person (there is no formal policy) to put into the business whatever private money he has. The program is intended for anyone going into or expanding a business who is unable to obtain the money from conventional lending sources.

The Globe-Democrat investigation, which involved two years of litigation by the newspaper under the Freedom of Information Act, entailed the examination of more than 14,000 loans, thousands of other documents, hundreds of interviews and a computer-assisted study of loan and default records. It was based on an analysis of nine years of direct loans made in 16 SBA offices.

Analysis of the SBA loan data was accomplished by utilizing the specialized computer systems and consultation services of Comshare Inc. an international computer services firm.

Among the findings:

Of the 14,261 SBA loans made in the 16 district offices from 1970 through 1978, 5,948—or 42 percent—have ended in default.

In terms of actual dollars lost, $157,535,380—or 33.3 percent of the $473,079,234 loaned during the period in the 16 offices—was never repaid.

SBA attempts to collect on collateral or force payment from loan recipients through the courts are minimal at best, with the agency collecting about 18 cents on the dollar once a loan has been placed in liquidation, the first step in writing off the loan.

Loans have been concentrated in small geographical areas marked by high unemployment and economic depression, yet within those areas the size of the loans made was significantly less than average overall. That pattern of relative undercapitalization gives weight to charges by dozens of minority loan recipients who told reporters they felt that heavily black areas were being given many of the loans to show "commitment" to the area, but that the loans were too small to allow a business to survive.

The SBA has consistently understated its loss rate, never admitting in any year between 1970–78 more than a 10.8 percent loss rate to Congress. Congress' watchdog, the General Accounting Office, has accepted as true and repeated with virtually no serious investigation the misleading loss rates.

SBA officials repeatedly increased the risk by making loans to people unqualified to run the type of business for which they have received the loan. Examples found by reporters include a barber who received a loan for a grocery store, a potato chip man who received a loan to run a liquor store, a clothing store salesman who received a loan to run a restaurant and a karate instructor who received a loan to set up an Oriental food store.

There has been a substantial hardship for those who received loans but soon discovered they were in well over their heads. Not only were life savings often lost as would-be entrepreneurs tried to keep their businesses afloat, but in a number of cases, reporters found people whose family life has been thrown into confusion and disarray due to the strain of debts, bankruptcy or loss of credit.

SBA officials failed to follow their own standard operating procedures—in making and monitoring loans and minimizing losses stemming from defaults—"in a push to get the money on the streets."

The high volume of loans and low rate of success within minority communities are exactly what the agency's regulations say should not happen. "From a socioeconomic viewpoint, the indiscriminate approval of loans at a high volume and low rate of success can do nothing but impair our relationship with the small business concerns and communities that we are attempting to help," the SBA's own procedures manual says.

Elsewhere in the manual, another major point is stressed: "Many loans are in liquidation solely because working capital requirements were not given adequate consideration."

So disorganized and troublesome is the program, in fact, that 11 of 16 district and branch directors interviewed in the 16 offices said privately that the entire program should be either scrapped or significantly overhauled.

"If we got a telegram tomorrow from Washington saying the direct loan program was being stopped, everyone in this office would stand up and cheer," said one Western district director.

Because of the large and representative sample size—the 14,261 loans examined are 26.8 percent of the loans made by the SBA from 1970 through 1978—the figures can be translated with statistical accuracy to reflect the national loss rate during the period, according to statistical experts.

In terms of dollars lost, the SBA default rate for the direct loan program is 33.3 percent, which means an actual loss of more than $571 million from 1970 through 1978. In terms of number of loans, the default rate is 42 percent.

Later years were not included in the study because there has been insufficient time for the businesses to show a pattern of either success or failure.

Loose practices lead to SBA's high failure rate

Loans often made to businesses sight unseen

By THOMAS L. AMBERG
and MICHAEL R. MONTGOMERY
Globe-Democrat Staff Writers

(Second of a series)

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Through its loose lending practices and servicing procedures, the Small Business Administration virtually ensures that its direct business loan program will have a staggering default ra'-, said dozens of field officials throughout the nation interviewed by The Globe-Democrat.

"It's not hard to see why there's such a horrendous failure rate for these businesses. It starts with a mentality that has no respect for the money it deals with," one official said.

That official San Francisco chief of liquidation Bernard Lump, recalled instructions given him by a former chief of finance in the New York City office. "He said, 'Don't look at it as money. Look at it as numbers on a computer run. We call them loans, but they're really just grants.'"

Asked why the default rate is so high as it is — 43 percent of the direct loans made from 1970 through 1978 failed — and what can be done about it, SBA field officers who were interviewed raised these major points:

● There is insufficient screening of applicants. "We lend money to whatever walks in the door," Lump said. "We should try to target our money to certain industries the way banks do."

Thomas Trimboli, district director in Phoenix, Ariz., said, "I'd like to see a more creative use of our direct loan money. Why not take most of the money and target it to the types of businesses that the state or city or area needs to ensure that it generates economic development?"

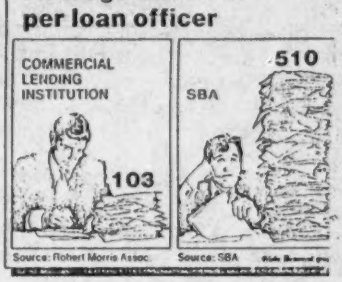
Such targeting is not possible because the agency's rules require taking loan applicants in chronological order on a first-come—first-served basis, Trimboli said.

Loan recipients' lack of business experience is cited as "the greatest single reason" for loan failure by most SBA personnel interviewed.

● Loans are made routinely without the loan officer or other SBA personnel even seeing the applicants' proposed or present place of business.

"Field visits are a MUST," Buffalo, N.Y., Branch Director Franklin J. Sciortino said. "You can't make a rational decision on a loan without a field visit. A picture's worth a thousand words, as the saying goes, and it's just

Continued on Page 6A



oose practices lead to SBA's high failure rate

Continued from Page 1A

zing how much you can tell about a
ness in just a five-minute visit."
nd yet, in every other office visited
eporters, officials conceded that
visits were not always made, and,
any cases, rarely made, because of
k of personnel.

BA's internal regulations require
field visits be made in all cases of
t loans to start a new business
s specifically waived by a loan
er's superior. The shortage of
onnel to handle the crush of
icants — waiting lists extend up to
ears — makes waivers the rule and
visits the exception.

SBA has for years marched out of
with the rest of the financial world.
ans are made throughout the year
rdless of financial conditions.
ding is a cyclical business, and we
ld treat it that way," said Lump, of
an Francisco SBA office.
When interest rates are high, we
ld be putting people into servicing
, not making them, and when
est rates are low, the reverse
ld be true.
But what happens is that SBA acts
ious to the wishes of the Federal
rve. When the Fed is trying to get
s and lending institutions to cut
on lending, the old SBA is right
there pumping more loans into its
illion portfolio. It doesn't make the
shred of sense," he said.

A major problem raised by
ral SBA field officials is the lack of
ific requirements for the borrower
t his own money into the business.

Although the SBA policy manual states that an "applicant must have a reasonable amount at stake in the business," there is no specific figure for private investment. The lack of a specific requirement for private equity by the applicant gives him little incentive to keep the business solvent, field officials said.

The chief financial officer in the Newark, N.J., district office advocated returning to the dollar-for-dollar matching concept used by the agency until the mid-1960s.

"You'd eliminate the type of situation where a couple of guys stand on a street corner one night and decide to go into business," he said.

Charles R. Hertzberg, director of the SBA's Office of Business Loans in the central office in Washington, said, "There was a weakening of the 7(a) loans (the major part of the direct loan program) to coincide with the EOLs (Economic Opportunity Loans, which are intended to help minorities and have never required a certain amount of private equity from the applicant.)"

● A sample of 534 loan files from 16 selected SBA offices showed that 33 percent of the loans were made in part or in whole to pay off amounts owed by the businesses to private or public creditors and to pay local, state or federal taxes.

In those cases, an average of 48.4 percent of the loan was used to pay creditors. Many times, the entire loan was used, with SBA approval, to pay off a series of private creditors.

In one case, for instance, the Dallas district office loaned $100,000 to a business that had failed six months previously. The loan went entirely to satisfy accounts payable, notes payable and a bank. The business (the Canton & Edgewood Concrete Co.) subsequently went out of business for a second and last time 3½ years later, with SBA losing about $55,000.

SBA regulations, however, dictate that loan proceeds may not be used to "bail out" any "creditors who are in a position to sustain a loss."

● From the same sample of 534 loans, The Globe-Democrat found 52, or 9.7 percent, that went in part to pay off other SBA direct loans. By doing so, the agency understated the actual number of defaulted loans.

Once a loan is approved, eventual failure and loss to SBA is often assured through policies that, in general, fail to protect the loan, investigation showed.

Those policies — or sometimes lack of policies — include:

● A shortage of personnel to service loans. Servicing personnel are theoretically supposed to handle a host of administrative problems, such as any changes in accounts, as well as be available to make calls on businesses in need of special help and attention.

Because the direct loan program is by its nature made up of higher-risk individuals, those businesses generally require substantial attention. However, the average caseload in the 16 offices surveyed by Globe-Democrat reporters is 510 loan recipients per loan officer.

In contrast, loan servicing officers at commercial lending institutions generally have a caseload of 10 to 100 cases, according to banking officials.

A recent study by Robert Morris Associates, the national association of bank loan and credit officers, found the majority of loan officers at commercial institutions handled no more than 99 loans. The average caseload was 103 loans per officer, according to the study.

Phoenix District Director Thomas Trimboli, discussing the high caseload, said, "The servicing people are not engaged in preventive management assistance; they're engaged in reactive management assistance."

Trimboli and other SBA field personnel complained that the lack of staffing makes it impossible for a servicing officer to do anything other than react to a crisis, not prevent one.

"Once the thing is failing, there's really nothing a government person or banker can do for it," said Lump, of the San Francisco office. "The bad decision was made in making the loan in the first place.

"Putting many of these people into business in the first place is like putting them in the ring with Muhammad Ali. Once they start to take a beating, there's not much we could do if we crawl in the ring with them," he said.

Another SBA official said, "It's pretty unrealistic to think a servicing officer can provide much real help when he has hundreds of firms to deal with."

● SBA fails to protect its collateral position in many cases. When a loan is made, the agency accepts certain collateral that is supposed to secure the loan. Often, the agency will later take a second position on the same collateral, thus allowing a commercial lender that comes along later to have first the residence or business prop giving SBA whatever, if anyth left over from a sale of that prop

"We don't protect our pos Lump said. "It's common. A guy going bad and wants more money, if the agency won't give it to him, goes out and gets it from a trust dee company. That company usuall charges interest at prime (rate) plu five points, plus another 10 to 24 point (a point is 1 percent of the loan amount on top of that for what's called loa origination fees.

"To make the loan, SBA has to agre to subordinate its position, and we do as a matter of course. Absolutely. W do about two a day in San Francisc and twice that in Los Angeles. It' rampant all over the country," Lum said.

Subordinating the loan positio means that when the trust dee company forecloses (which almo always happens, according to Lump SBA is left with no collateral return "Millions go down the drain in th way," Lump said.

NEXT: *Inexperience no bar to loan*

evenue-sharing ay get budget ax

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How SBA Loan Cooked Up Restaurant Failure

(By Thomas L. Amberg and Michael R. Montgomery)

Merrill L. Moss, a self-described amateur cook with no experience in operating a restaurant, opened a posh eating establishment in St. Louis with $150,000 of taxpayers' money and flopped less than 6 months later.

With all but $5,996 lost, Moss closed the gourmet dining establishment at Fourth and Olive streets called Chez Jean Pierre, which had offered main meals from Coquelet Albufera at $15 to Carre d'Agneau en Croute, the house specialty, for $37.

Moss told The Globe-Democrat that from the beginning in 1978 he had no experience in the business "whatsoever" to back up his "glamorous" venture.

"You and all other taxpayers paid for my failure," he said.

Moss' experience is one example of how the Small Business Administration—through poor procedures for making loans, monitoring them, and minimizing taxpayer losses when default occurs—has lost one-third of the $2 billion it spent during the decade ending in 1979, a Globe-Democrat investigation has revealed.

The performance record of the St. Louis SBA office serving eastern Missouri is one of the worst in the nation, reflecting the failures of a program whose cost is much greater than the hundreds of millions of dollars lost through defaults, The Globe-Democrat investigation showed.

A rush to "get the money on the street," as one SBA official described it, has resulted in St. Louis officials making loans almost haphazardly to people who, by their own admission, were totally unqualified and inexperienced to run the businesses being financed at taxpayers' expense. As a result, almost six of every 10 loans of the 1,041 loans made here from 1970 through 1978 have ended in default.

Although the SBA's policy and procedures manual stresses that the management ability of the prospective borrower is a prime factor in considering an application, SBA officials have often given loans to people who were making major career changes without benefit of prior experience.

And, in many cases, the businesses were so short-lived or did so poorly that because of accruing interest and lack of payments, the SBA is owed more money than it loaned.

The loan failure rate here not only raises questions about the qualifications of the borrowers but the qualifications and procedures of SBA personnel as well.

The ill-fated venture of Chez Jean Pierre is one of many examples.

On May 15, 1978, the SBA approved the $150,000 loan to Moss to set up Chez Jean Pierre—despite the fact that, as Moss said, "I had no experience whatsoever. Nothing. I'm an amateur cook, and it seemed like a sort of glamorous concept."

A former advertising writer, Moss recalled the whole venture as a nightmare, with the bottom line being that he opened in November 1978 and closed less than six months later on May 1, 1979.

With SBA's blessing, he said, he had selected a "terrible location," had accepted a financing proposal that left him woefully short on working capital and got into a business he knew nothing about.

The cost to the SBA, and ultimately the taxpayers, was $144,004 in principal and interest that the SBA has had to charge off. Moss filed for bankruptcy, and the debts were discharged by court order.

Today, living in Barnbridge Island, Wash., Moss said, "They would have done me a huge favor if they had turned down my loan and told me to go get some experience before I try it on my own."

Examples of SBA failures—in which 33.3 percent of the $2 billion spent on the program from 1970 through 1979 ended in default—are legion.

From February 1970 to April 1971, the SBA here made three loans—the first for $10,000, the next for $25,000 and the third for $65,000—to Luther Boykins, a barber, to open Luther's Market, a grocery store at 4135 Shreve Ave. Six months after the final $65,000 loan, the grocery shut down, Boykins went back to being a barber, and the SBA was left with $79,183 still owed in principal and interest. That amount was subsequently charged off.

Boykins said he is bitter that the SBA even gave him the loan in the first place, because besides losing his life savings, he incurred a debt he said he will never be able to pay off.

"I was going to be a failure no matter what," he said. "The combination of a lack of experience and a lack of working capital doomed me."

The SBA did not inspect the stock or equipment, provided no advice on taxes, management or bookkeeping and offered no aid from SCORE (Service Corps of Retired Executives) volunteers, he complained.

He maintained that the SBA's direct loan program amounts to no more than "pacifying and satisfying" the black population, and is, in fact, "designed for black people to fail" because it sets them up in business without the proper experience or enough financing.

When William J. Herbster applied for an $8,000 SBA loan on May 2, 1972, he was a potato chip salesman on a truck route. Nine days later, when his loan was approved, he was the new owner of the Driveway Liquor Store at 4114 Jennings Road, Jennings. Five months later, he was out of business, leaving the SBA with $8,463 in principal and interest to charge off as another bad debt.

Herbster remembered that he "went down to see the man at SBA (to ask for a loan), and it was all real quick. They gave me the money right away," despite, he said, his lack of experience.

In another case, M.C. Skinner, with a background of 20 years in retail clothing sales, was given $32,400 in loans to turn a deserted gas station on the city's North Side into a diner.

Although SBA officials suggested Skinner might look into the idea of his own clothing shop, he insisted it was "a dying business," he said, and remained set on the idea of his own diner.

Skinner received a $29,400 loan from the SBA in December 1978 and another $3,000 loan in September 1979.

After 14 months of delays, occasioned in part by misinformation from SBA officials, Skinner said he finally opened his restaurant at 2914 Parnell Ave. in February 1980. But the business went bust in September 1980, leaving Skinner with no diner, no credit rating and the loss of at least $2,500 of his own money.

The SBA, and taxpayers, were out a total of $34,566 in principal and interest.

One West End restaurant at 5897 Delmar Blvd. with the catchy name of Tak-It-An-Gitt received a loan in 1971 for $10,500. Today, the SBA has long since written off the loan, with Tak-It-An-Gitt still owing $10,471.88 in principal and interest. The interest stopped accruing in 1976 when the loan was written off. Globe-Democrat efforts to reach the owners were unsuccessful.

When auto mechanic Franklin Williams "was looking around for something to do" in Philadelphia in 1971, he and his cousin, Dillard Mosley, a salesman for Sears Roebuck and Co., thought opening a hardware store would be a good idea. He told The Globe-Democrat that he and his cousin put together some projections ("we didn't exactly know what we were doing") and presented them to the SBA.

SBA thought the idea was a good one, and without changing anything in the projections, gave Williams $50,000 to buy Feldman's Hardware Store.

"The projections were way, way off," Williams said. "We knew we were in trouble within a year. The store lasted 3½ years." He said he is again working as a truck mechanic and his cousin is "somewhere out West."

Ye Mo Ahn was a karate teacher in 1975 when she decided that "the karate wasn't going so good." Some friends told her that they thought "an Oriental food store would go good, so I tried it." With no managerial experience, she could only keep the store afloat 1½ years on the $30,000 SBA loan before "too much competition killed the business," she said.

Similar versions of one phrase—"getting the money on the street"—cropped up again and again in Globe-Democrat interviews with SBA officials in 16 offices nationwide.

The phrase represents what many—including SBA officials—regard as a bureaucratic distortion of the program's original intent of helping individual entrepreneurs become successful businessmen, but has come to be viewed in terms of how many billions of taxpayers dollars have been doled out.

Defaults Here Among Highest

The St. Louis Small Business Administration's office has one of the highest default rates in the country in its direct loans to aspiring businessmen.

From 1970 through 1978, the local office made 1,041 loans, and 582—or 55.9 percent—ended in default and out of business.

Of the 16 SBA offices selected in The Globe-Democrat's investigation of the agency's direct loan program, only Cleveland had a higher default rate—54.46 percent of the 859 direct loans made during the same period ended in default.

In St. Louis, the direct loans during the same period totaled $22,850,945. More than 52 percent of that amount went to the 582 firms that ended in default and out of business. Subsequently, the SBA, and taxpayers, look a loss on 82 percent of the money loaned to those firms. A total of $9,765,739 was charged off as a loss by the

SBA here, and another $561,711 in interest owed on the loans was also written off as a loss.

The Globe-Democrat investigation chose the years 1970 through 1978 because of the high volume of loans and dollars in the program during that period. Most of the SBA loans are for a 10-year period.

For the period chosen, business failure rates were high for the first few years and then declined in the more current years. The default rate here reached 69 percent in 1971; more recently it has been as low as 26 percent. The rate declines in more recent years not because SBA policies or procedures have improved, but because the businesses have not been in the program long enough to determine their ultimate success or failure.

The failure rate in St. Louis by year is: 1970, 56 percent; 1971, 69 percent; 1972, 68 percent; 1973, 65 percent; 1974, 48 percent; 1975, 51 percent; 1976, 38 percent; 1977, 41 percent; 1978, 26 percent.

Analysis of the SBA loan data for the 16 SBA offices was accomplished by using the specialized computer systems and consultation services of Comshare Inc., an international computer services firm.

St. Louis Globe-Democrat 9/5/1

Globe-Democrat Photo by John Dengler

Elizabeth Taylor stands in front of the boarded-up midtown St. Louis building that housed her ill-fated restaurant.

Tales of ruined businesses — and lives

By THOMAS L. AMBERG
and MICHAEL R. MONTGOMERY
Globe-Democrat Staff Writers

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(Fourth in a Series)

"I can't tell you how it would have helped my life so much if they had never given me the damn money. All it did was ruin my life."

The price of failure was high for Elizabeth Taylor, who started a midtown St. Louis restaurant with a Small Business Administration loan and then watched it close.

An SBA-commissioned consultant had advised against the loan, citing a poor location, insufficient capital and her lack of business experience in concluding that the venture would be "perilous."

A TOP OFFICIAL at the SBA office here agreed, saying the $88,900 loan was "not adequate."

But less than three weeks later, the SBA granted Mrs. Taylor a loan for $36,700 — less than half the original request. A bailout loan of $32,000 followed the next year in 1975, but the money was not enough — Mrs. Taylor closed her business last year.

She now lives on a small medical disability payment and food stamps.

Mrs. Taylor is one example of the failures of the SBA's direct loan program, in which tax money — an estimated $571 million was lost to defaulted loans from 1970-78 — is not the only cost, and taxpayers are not the only victims.

People who applied for loans came to the SBA office here with ideas that represented their lives' ambitions — a chance to run their own businesses, to be independent, to stand on their own feet and to be their own bosses.

BUT IN MANY cases, often when SBA officials did not even follow their own rules and regulations, people who were successful in obtaining the loans not only lost their businesses, but their life savings, their homes and their credit ratings. In one case, a man even lost his family.

When Willie Smith walked into the St. Louis SBA office to apply for a loan to run a small grocery store, he was justly proud of himself. He was, he said proudly, one of the first blacks to be hired as a meatcutter by a St. Louis grocery chain, and he had worked steadily at the trade for 12 years, adequately supporting his wife and four children. Now he was ready to go to work for himself, running a meat and grocery store.

But at the SBA, no one seemed to know anything about setting up a grocery, and the $28,000 loan he received proved totally inadequate, he said.

"BY THE TIME we bought stock and paid regular monthly bills, there was nothing left to operate on. We (Smith and a partner) had chosen a bad

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...orrowers tell of ruined businesses — and lives

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ation, but we didn't know any better. ...did about $3,500 in sales each week, ...a feasibility study done a year after ...opened said we'd have to pull in ...,000 a week in sales to survive. We ...er got over $5,000," he said.

...Smith's operation, the Specialty ...at Co. at 4261 Maffitt Ave., soon ...ed downhill. A move to a second ...ation, 1424 Dielman Road, Overland, ...ved no more successful because of ...lack of adequate working capital, he ...d.

"We were always in debt, never able ...restock properly and always living ...d to mouth," he said. "There was ...er money to make any payments to ...SBA."

"It's the blind leading the blind," ...ith said bitterly. "If they (SBA ...erals) don't know any more than I ...they're not much help. It's nice they ...e me the loan, but it's no help if they ...'t help me succeed."

...Smith's business went further and ...ther into the red, despite Smith's ...rking more and more hours. Debts ...d frustrations began to take their toll ...n pressure on the family, he said.

"MY WIFE couldn't take the ...ssure of the debts, and we ended up ...parating. The whole thing created a ...of hardship for the family. It really ...e us up," he added.

...Smith's business, started in late ...6, folded in mid-1978. Smith now does ...ld jobs" and cuts meat when extra ...hs needed. He said he takes most of ...pay in groceries and then takes ...m to his estranged wife and ...ldren.

"I tried to get a loan to do better in ...life, but I got a loan and ended up a ...worse. I guess I've learned a lot," he ...d.

The price also was high for Mrs. ...lor, a St. Louisan who for years ...ore receiving an direct loan had run ...mall but successful catering business ...of her North Side home.

"When I applied for that first loan in ...6, my world was going pretty good. I ...about $35,000 of my own money, a ...se with a mortgage that I had paid ...n from $21,000 to $9,000, a car and ...d health," she said.

"But afterward, after getting the ...n and all that followed, I had lost my ...ney, my home, my business and my ...lth. The emotional strain of fighting ...ough this horrible thing has just torn ...family apart emotionally. My oldest ...got so upset over the business ...ure that he had a breakdown," she ...d.

"I can't tell you how it would have ...ped my life so much if they had ...er given me the damn money. All it ...was ruin my life," she said.

IN FACT, THE SBA turned down ...Taylor's original request for an ...,900 loan, in part based on the ...dings of a feasibility study ...missioned by the SBA to look into ...Taylor's idea of a restaurant and ...ering service at 3536 Washington ...

That study, obtained by The Globe-...mocrat, stated, "This total concept ...ears unrealistic for this area of St. ...is at the present time due to the fact ...t it is a transitional area and the fact ...t Mrs. Elizabeth Taylor has little ...nagement and business experience ...for such a large operation."

Globe-Democrat Photo by John Dengler

Willie Smith, one of the first blacks to be hired as a meatcutter by a St. Louis grocery chain, works at a confectionery at 3701 Cook. "I tried to get a loan to do better in my life, but I got a loan and ended up a lot worse. I guess I've learned a lot," he said.

The report called Mrs. Taylor's proposed venture "perilous" and "high risk" because of the location and her lack of business experience.

And, in declining her request for $86,900, S.C. Slaughter, then chief of SBA's financing division, wrote that the loan could not be approved because, "Working capital of $23,900 after the loan is not adequate to sustain the operation during its development stages."

So what did the SBA do for Mrs. Taylor? Less than three weeks after Slaughter's letter, Mrs. Taylor received a loan for $36,700 for essentially the same operation she envisioned in the $86,900 loan. The $36,700 loan left Mrs. Taylor with only $3,700 for working capital, according to SBA records.

A SECOND loan the next year for $22,000 ended up being used largely to bail Mrs. Taylor out of debts rapidly incurred from the small capitalization in the first loan, records show. The loans were put in liquidation status within two years after they were made, and the business sputtered along for five years before closing in August 1980.

In fact, even though the loans went into liquidation on May 25, 1978, the SBA made no attempt to collect on its loan. The loans were officially charged off on Feb. 23, 1978, records show, again with SBA making no attempt to collect anything. For more than two years after being "charged off" SBA continued to ignore the debt.

By the time the agency finally moved to collect anything on its loan, the business had little left of value, and SBA collected absolutely nothing from the sale of business chattels, giving the sum to the auctioneers instead.

In the case of Lionel E. Lefler, an American Indian who wanted to open a health club, it was a similar story.

LEFLER HAD been and still is a high school physical education teacher. He thought he would have no trouble running a health club in the Oakville Shopping Center in South St. Louis County.

Once he got his $61,000 loan, he had no problems with the SBA and very little contact with the agency, either, he added.

But problems began even before the club opened, Lefler said, when the landlord of the shopping center placed the club in the rear of the complex, not in the front as Lefler had been led to believe.

"It was a poor location, but I didn't realize how bad it was at the time. Maybe if the SBA had given me some management training, I might not have let this happen," he said.

But, Lefler said, he was offered no such courses or help despite the SBA mandates that all borrowers without management experience, such as Lefler, receive management assistance training.

In fact, Lefler said, he wanted to wait until he could get a better location because his application for the loan had been predicated in part on a choice site for the club. But because the loan had already been approved, he said, an SBA official told him not to wait but to take the money and work with the less desirable location.

LEFLER'S HEALTH club opened in early 1978 and lasted a little less than three years. During that time, he received only one visit from SBA officials — "and they were in an obvious hurry to leave," he said.

Although Lefler twice requested and received a moratorium on his loan payments, no SBA official contacted him about his business problems.

He said he once called the Service Corps of Retired Executives, a group of retired businessmen that offers management help to SBA borrowers, but was told no one there knew the physical fitness business and "then they told me to call back in a few months if things didn't get better."

When the business folded in 1980, the SBA had put in a total of $63,000 and Lefler had lost $20,000 of his own money, including a house he had owned.

When he thinks back on the venture, Lefler is not bitter and he does not put all the blame on the SBA. Nonetheless, he would change the past if he could.

"I'd have been a lot better off financially if they'd have told me no — hell no."

NEXT: Stacking the deck against minorities

Reprints on sale:
Reprints of this series will be available in booklet form in two to three weeks. Mail orders can be sent to: SBA Reprint, St. Louis Globe-Democrat, 710 N. Tucker Blvd., St. Louis, Mo. 63101. The first copy is $1.25, each additional copy in $1. Checks should be made payable to St. Louis Globe-Democrat.

St. Louis

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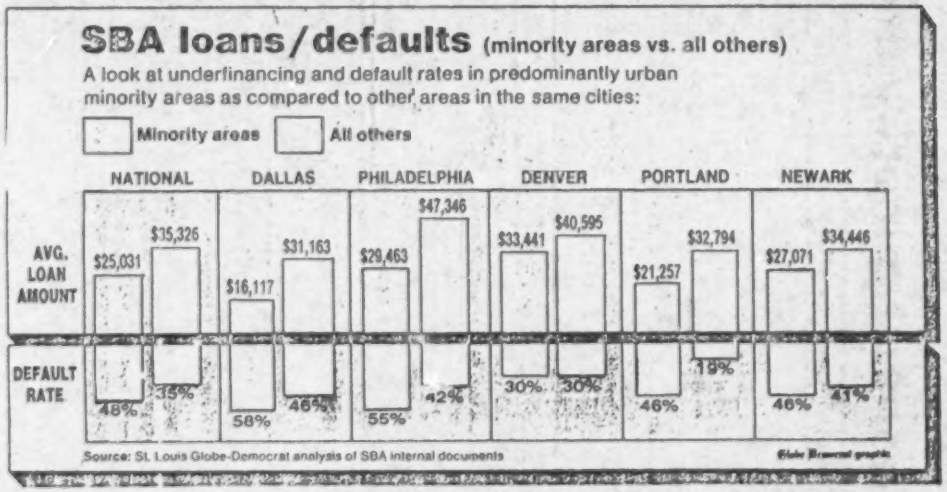

Deck is stacked against minority areas

By THOMAS L. AMBERG and MICHAEL R. MONTGOMERY
Globe-Democrat Staff Writers

(Fifth of a series)

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The Small Business Administration has given smaller loans to borrowers in depressed minority areas than to aspiring businessmen in surrounding regions, stacking the deck against the survival of enterprises in the minority areas, a nationwide Globe-Democrat investigation shows.

[illegible] averaging 41.1 percent more than businesses in depressed, minority areas under the Small Business Administration's direct loan program.

And yet minority businessmen argue [illegible] insurance costs, higher security costs and renovation and leasehold improvement costs.

THE PATTERN OF granting smaller loans makes economic survival more difficult for the type of businesses that the SBA's multibillion-dollar direct loan program is designed to foster, the investigation shows.

The smaller loans to minority businesses correspond closely with the higher default rate in minority areas. The Globe-Democrat's investigation [illegible]

with only 35 percent of the direct loans in predominantly white areas.

The underfinancing in minority areas was disclosed by a computer analysis of 14,261 loans representing 26.8 percent of the more than 51,000 direct loans granted nationwide from 1970 through 1978. Estimates of nationwide performance were based on that sample, representing all defaults in 16 cities in that period.

IN ANALYZING the data, The Globe-Democrat used the specialized computer systems and consultation

SA St. Louis Globe-Democrat Fri., Sept. 4, 1981

Deck stacked against minority areas

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in predominantly black or Hispanic areas was $25,031 — but the average in all other areas was $35,324. The difference of $10,293 represents a 41.1 percent disparity.

The Globe-Democrat examined the direct loans made from 1970 through 1978 in 16 district offices throughout the country: St. Louis; Phoenix, Ariz.; Detroit; San Francisco; Portland, Ore.; Atlanta; Miami; Minneapolis; Dallas; Cleveland; Philadelphia; Buffalo, N.Y.; Denver; Newark, N.J.; New Orleans; and Washington. The disparity in some district offices, which generally cover either all or a major portion of a state, was particularly acute.

IN DALLAS, for instance, the average SBA loan made in predominantly black and Hispanic areas was $16,117, but the average loan in all other areas of Dallas was $31,163 — or 93 percent more.

In Philadelphia, the average loan in black areas of the city was $29,463, but the average loan in all other areas was $47,346 — or 61 percent more. The situation was the same in the 16 offices. In each case, areas of high minority concentration received less than predominantly white areas.

Not only has the SBA given smaller loans to minority businesses, it has compounded the problem by concentrating high-risk types of businesses in the depressed areas. In fact, the agency's direct lending portfolio has been heavily concentrated in six types of businesses: bars, restaurants, food stores, cleaning shops, clothing stores, and truck hauling firms.

Businesses receiving most SBA loans

National		St. Louis	
1. Restaurants	1,385	1. Food stores	120
2. Bars	1,121	2. Restaurants	112
3. Food stores	1,071	3. Bars	104
4. Apparel	896	4. Truck Hauling	120
5. Laundry/Cleaning	661	5. Laundry/Cleaning	73
TOTAL	5,134	TOTAL	529

THOSE SIX TYPES of businesses accounted for 41.6 percent of the 14,261 loans reviewed by The Globe-Democrat, with more than 350 other types of businesses accounting for the remaining 58.5 percent of SBA direct loans.

Leading the list in terms of numbers of SBA direct loans were restaurants, which received 1,385, or almost one in every 10 loans. Next were bars, which received 1,121 loans, and food stores, with 1,071 loans.

In St. Louis, for instance, although the SBA office made loans to 231 different types of businesses during the period 1970 through 1978, 48 percent of all defaults during that period occurred in those six types of businesses, records show.

The SBA office here and other offices around the nation are seemingly oblivious to the high risk and low need for these types of businesses, but nonetheless continue to finance new bars, restaurants, grocery stores, cleaning shops, clothing stores, and truck hauling firms — and each year more of these same businesses end in failure.

SBA loans for new businesses have been concentrated in a small portion of North St. Louis, Wellston and Kinloch.

This concentration has lead to a higher SBA loss ratio (defaults as a percentage of disbursements), pumping hundreds of new businesses into areas where it is difficult to support them economically. The result is a higher loss rate for the SBA and financial hardships for those people receiving the loans in the depressed areas.

OF 582 LOANS that ended in default during the period 1970 to 1979, slightly more than 50 percent — 293 loans — were from a two-square mile area in the northern metropolitan area of St. Louis representing only eight ZIP codes. The St. Louis SBA district office makes loans throughout Eastern Missouri.

In comparison, the rest of the St. Louis metropolitan area — representing 44 ZIP codes — accounted for only 38 percent of loan defaults.

The computer analysis by Comshare Inc. confirms what dozens of loan recipients from the northern St. Louis metropolitan area told Globe-Democrat reporters during interviews: Loans within the predominantly black areas were significantly smaller in comparison with loans made in surrounding, predominantly white areas.

The average loan amount in the predominantly black areas reflected was $17,871, while the average loan in the rest of the St. Louis metropolitan area was $23,496 — or more than 31 percent greater. Computer analysis by Comshare shows no statistically significant difference in the types of businesses in both areas.

That means that while the same types of businesses received loans in both areas, those in predominantly black areas received less capital for their companies than fellow entrepeneurs in surrounding areas.

FOR EXAMPLE, of 67 defaulted loans to restaurants in the St. Louis area, 36 were in the northern portion of the city, and 29 in the entire rest of the metropolitan area. While the average loan amount to restaurants in minority areas was $16,969, restaurants in the rest of the metropolitan area received an average loan of $27,991 — or 65 percent more — and suffered a smaller default rate.

The same pattern is true with food stores, where the average loan made to the 41 stores that defaulted in the northern portion of the metropolitan area was $21,400, while the average loan made to the 15 defaulted stores in the rest of the metropolitan area was $27,496 — or 28 percent more.

"From a socioeconomic viewpoint," says the agency's procedures manual, "the indiscriminate approval of loans at a high volume and low rate of success can do nothing but impair our relationship with the small business concerns and communities that we are attempting to help."

The manual also stresses that "many loans are in liquidation solely because working capital requirements were not given adequate consideration."

SBA OFFICIALS throughout the nation acknowledge the concentration of loans into the few types of businesses, but argue that because of the agency's policy of accepting loans in chronological order they have little or no control over which businesses get loans.

Additionally, they say, the six categories cited are "entry" type businesses that are common for people starting a business. Many SBA officials add, however, that they would prefer a system that would enable them to select loans for businesses based on the needs of the community and on the quality of the applicant, not just on a first-come, first-served basis, as required by their procedures manual.

More than $74 million was loaned into minority areas while nearly $400 million went into all other areas, according to documents from the 16 SBA offices. More than 2,900 loans were made in minority areas, and more than 11,000 went into other areas.

NEXT: Dollars out, pennies back.

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St. Louis Globe-Democrat 7/6/81

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SBA gets pennies from dollars it's owed

By THOMAS L. AMBERG
and MICHAEL R. MONTGOMERY
Globe-Democrat Staff Writers

(Sixth of a series)

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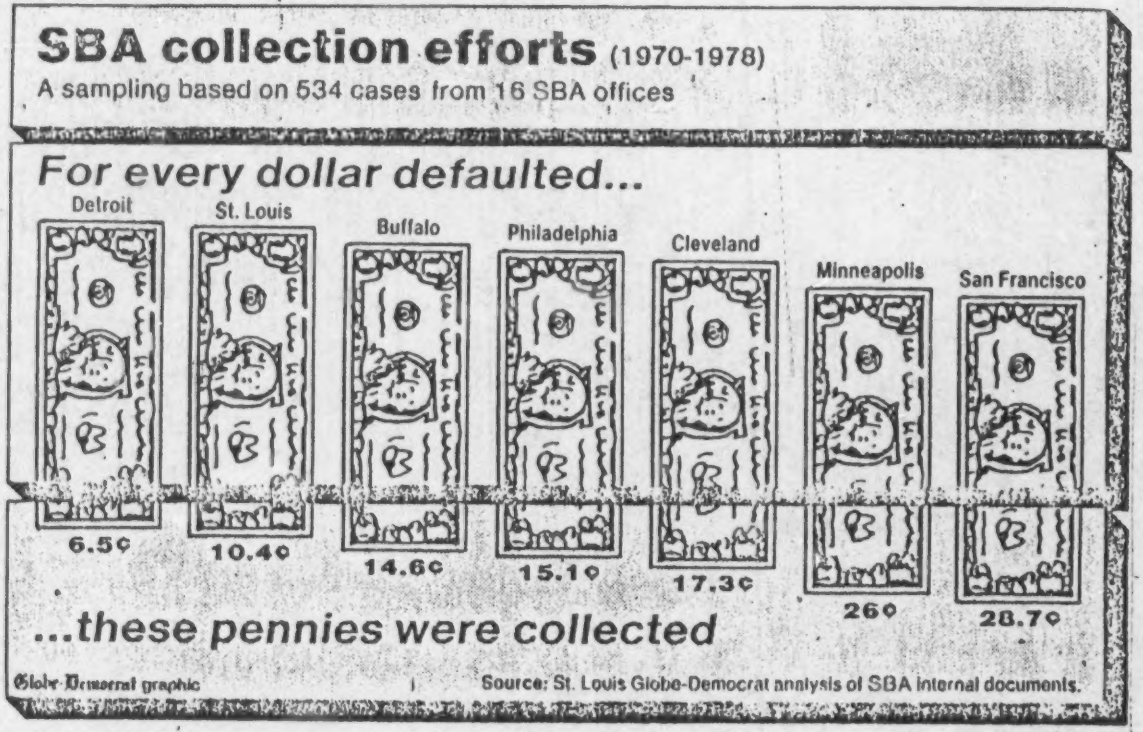
The Small Business Administration collects just pennies on every dollar it is owed in direct loans from businesses that close down, despite regulations requiring "maximum recovery."

Collateral — land, buildings or anything else pledged by a borrower to secure the loan — is often grossly overstated, and, in some instances, is actually non-existent, records show. Collection efforts proceed slowly, and large sums are routinely written off without filing suit against the debtor.

Nationally, a survey of 534 files from 16 SBA offices throughout the nation shows that SBA collects just 18 cents on every dollar it is owed at the time a loan is placed in liquidation status. In some offices, the rate of collection is even lower. The SBA offices selected serve not only their metropolitan areas but all or major portions of their states.

IN DETROIT, FOR instance, records show that the agency collects just 6½ cents on each dollar it is owed

Continued on Page 15A



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SBA gets just pennies from dollars it's owed

Continued from Page 1A

at the time a loan is put into liquidation. In St. Louis, 10.4 cents per dollar owed is collected; in Buffalo, N.Y., the figure is 14.6 cents per dollar owed; and in Philadelphia, 13.1 cents per dollar owed is collected.

Two major causes for the poor collection have surfaced in discussions between reporters and SBA field personnel in the 10 offices: the widespread practice of deferring loan payments for borrowers who fall behind in their payments; and the easy willingness of the agency to allow other and later creditors to take a higher priority in their right to collect in the event of a default.

The practice of deferring loan payments, called "gaming" by some SBA officials, often is done to make an SBA officer's loan portfolio appear to be more "current" (that is, to have fewer loans in a delinquent status). The deferred loans often are to businesses that are clearly failing, according to field personnel interviewed.

BY ALLOWING A recipient to defer payments to the SBA, there is often simply a reduction in cashable assets over the period of deferment rather than a saving of the business enterprise — with SBA ending up with little or nothing left in a business to collect on.

The second major cause of poor collections is the willingness to subordinate the agency's lien position on real property, those interviewed said. This puts the SBA in a poorer legal position to collect than other, later, creditors.

The result, once a business fails, often leaves the agency with no meaningful collection rights. But the new lender, charging high interest rates, makes thousands of dollars for five or six months of participation as a result of its better collection position.

IN SOME CASES, the reasons for lack of collection are unclear. What is clear, however, is the small return to SBA.

Some examples:

On July 21, 1972, the SBA approved a $500,000 loan to the Martin Luther King Jr. Plaza Corp. in Cleveland. That loan, for a shopping center, was secured by a first mortgage on the land and buildings owned by the borrower, assignment of rights, title and interest in a lease agreement, and guarantee of lease payments of $10,000 a year for 10 years to SBA.

On April 26, 1973, another $21,000 was loaned to the Plaza Corp. Less than a month later, another $82,000 was loaned to the corporation. Four days later, another $43,430 was loaned, and one week later, another $100,000 was loaned to the Martin Luther King Jr. Plaza Corp.

That, however, did not end the federal largesse to the corporation. On Sept. 24, 1973, the agency loaned it another $82,917, and followed it up in May 1975 with a seventh and final loan of $82,930. In all, the Martin Luther King Jr. Plaza Corp. received $703,277 from the SBA.

Slowly, but surely, however, each loan went into default, and the borrower repaid the SBA a total of only $4,348 of the $703,277 loaned. The agency was left holding the bag for another $698,344 in interest, which was written off with the principal for a total of $880,873.

What has the SBA collected on its business property collateral, its lease agreements and its guarantees from Plaza? $0.

The SBA made no attempt to collect, but still holds the mortgage paper, which officials now describe as virtually worthless.

On April 5, 1973, the Dallas office of the SBA approved a loan of $160,000 to the Meridian Industrial Foundation Inc., as a partial financing of a $260,000 motel and restaurant project.

To secure its investment of $160,000, however, the SBA accepted a second lien on the land and buildings of the 24-unit motel and restaurant, a second security interest on the machinery, equipment and furniture, and rights to a portion of equity in a lease purchase agreement.

But when the loan ended up in foreclosure, the first lien holder collected. SBA collected nothing.

On Dec. 3, 1976, the Newark, N.J., office of the SBA loaned $76,600 to the Strickland Corp. to operate an automotive repair shop. The loan was secured with a first security interest in the machinery, equipment, fixtures, furniture and inventory, as well as a first mortgage on the business real estate.

Yet when the business closed down four years later, SBA liquidation officers collected a grand total of only $187.30 and were forced to charge off $77,842 in principal and assessed liquidation charges.

On Nov. 13, 1972, the Miami SBA office approved a loan of $31,800 to the Bryant Trucking Co. with the collateral to include a first lien on unimproved lots in Palatka, Fla., and a first lien on two new Chevrolet dump trucks. The dump trucks were bought for more than $31,000, according to SBA records.

But just 21 months later, when the loan went into liquidation, the SBA allowed the borrower to sell one of the trucks, and the agency sold the second one at a public sale. The total netted by the agency for the 21-month-old dump trucks was just $7,534, records show. The SBA did not try to collect anything from the land.

Literally hundreds of cases reviewed contained similar failures to collect on collateral or failure to require a lien position better than second or third position on collateral, which in most cases prove worthless to the agency in recovery attempts.

THE HIGHEST collection rate of any of the 10 offices surveyed was in San Francisco, but even there only 38.7 cents was collected on each dollar owed at the time of liquidation.

The Globe-Democrat's examination did find a regional disparity in collection rates, with the Western offices collecting more per dollar than offices in the rest of the nation.

Western SBA officials say this is a result of using deed of trust foreclosure proceedings on real property. The procedure allows a lender to bypass the necessity of going to court and allows it to obtain a summary foreclosure using a deed of trust. The result is faster and easier collection on real property, which is usually the bulk of collateral.

In the East, on the other hand, collections are complicated by a general lack of deed of trust laws to allow the same summary foreclosures used in the West. And there is a lower per capita rate of home ownership in the East than in the West, some SBA personnel say. With more apartment dwellers, the average loan is secured by less real property.

IN THE CENTRAL state offices, there is a mixture of collection rates brought about, apparently, SBA personnel say, by differences in work ethic.

"I really think there is a regional ethic," Denver District Director Chester B. Lendrum says. "It has to do with the type of people, and geography has to do with high recovery rates in liquidation. It starts to break down when you get into the large urban areas. The rural states are far better," he says.

Statistically, at least, Lendrum's comments are borne out in The Globe-Democrat's survey. The Minneapolis district office's collection rate is 35 cents on the dollar, while other, generally urban, states in the central area average far less. Detroit collects 6.5 cents on the dollar; Cleveland collects 17.3 cents per dollar; and St. Louis collects 10.4 cents per dollar. The more rural Western states also have a higher collection rate, as does the rural South, while the industrial East and Central offices lag behind.

But SBA field officials say the basic cause of collection failures goes back to the failure to adequately secure the loan in the first place, and the lack of enough staff members to monitor the loans.

NEXT: Hiding the truth from Congress

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BA figures mislead Congress on rate of defaults

By THOMAS L. AMBERG
MICHAEL R. MONTGOMERY
Globe-Democrat Staff Writers

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(Seventh of a series)

U.S. Congress was given reports ning misleading and out-of-date ates on direct loans by the Small ss Administration throughout the a Globe-Democrat investigation d.

le the agency was losing one of every three it loaned to ssmen in the direct loan program 1970 through 1978 — totaling an

estimated $571 million — it never admitted in reports to Congress a loss rate greater than 10.8 percent.

THOSE MISLEADING and understated SBA figures on default rates were accepted without question by the General Accounting Office, Congress' investigative arm, and passed on as fact.

As a result, elected officials have never been given a true and up-to-date picture of loss rates for the quickly deteriorating program, and there has been little concern over loans that have failed far more often than believed. Indeed, misinformed about the magnitude of the losses, Congress has repeatedly increased financing for the program.

SBA reports to Congress from 1970 through 1978 consistently understated loss rates by presenting financial data in such a way as to minimize losses from the $2 billion put into the program during the 1970s, a Globe-Democrat investigation showed.

SBA officials were able to paint an optimistic picture of the direct loan program losses every year by using cumulative default figures for the life of the program, extending back to the Eisenhower era. This obscured high losses for the last decade by merging the loss rate for any given year into the average loss rates for the early years.

SBA REPORTING practices made it virtually impossible to assess the performance of the SBA during any given year.

When the rates are averaged together, the low dollar loss rates for the earlier years serve to hide the serious deterioration of the program during the 1970s. As a result, the SBA has been telling Congress that the program's dollar default rate was 10.8 percent when, in fact, it was more than three times that high — 33.3 percent —

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SBA default figures mislead Congress

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as revealed by The Globe-Democrat's investigation.

In terms of numbers of loans defaulted, the default rate was even higher — 42 percent.

Not only has SBA's loss rate reporting technique kept Congress in the dark, it has kept SBA from knowing what has been happening.

When reporters asked SBA officials about the loss rate during the 1970s, they were told that the agency did not know what it was and that the agency was unable to check what happened to loans made in any given year.

Reporting only cumulative figures blurs the impact of sharply higher default rates and thereby creates little accountability for the effect of specific policies.

CHARLES R. Hertzberg, director of SBA's Office of Business Loans, acknowledged that point to The Globe-Democrat, saying, "Admittedly, your method (The Globe-Democrat method of tabulating loss rates by year) would give us a better reflective picture of the effect of our various loan policies."

SBA also failed, and still fails, to report the default rate in terms of numbers of loans — a more significant figure in a program that is designed to help individuals.

The newspaper obtained SBA loan data and files on 14,261 cases throughout the nation under the Freedom of Information Act. The data was analyzed by using the specialized computer systems and consultation services of Comshare Inc., an international computer services firm.

Congress expects to be informed of the progress and problems of the Small Business Administration by the General Accounting Office. But when reporters turned to GAO reports for statistics on loan loss rates, the figures they found turned out to be those passed on from the SBA without confirmation or checking by the GAO.

For instance, a GAO report on Aug. 21, 1979, into the 7(a) direct loan program (one of four business loan categories that make up the direct loan program) carried figures for loss rates for 1975 through 1978 after noting that "SBA's loss-rate figures, for all district offices, for fiscal years 1975-1978 follow . . ."

WHAT CAME NEXT was a listing of years and loss rates, with 1975 listed as having a loss rate of 6.42 percent; 1976, 6.51 percent; 1977, 6.50 percent; and 1978, 6.61 percent.

What the GAO report failed to mention was that the loss rates were not in fact loss rates for each year, but were cumulative totals for all years up to the year cited, and that the figures were not the result of its own study, but were supplied by SBA.

Henry Eschwege, director of GAO's Community and Economic Development Division, which supervises GAO reports, acknowledged to The Globe-Democrat, "We do often have to rely on data from the agencies, but when we find discrepancies, we'll use our own figures."

Although Eschwege said GAO routinely runs "reliability studies" on figures given it by various agencies before including the figures in its reports, an assistant, John Landicho, said that no such studies were undertaken on the SBA default figures, which passed directly from the SBA into GAO reports without questions.

When Globe-Democrat reporters asked GAO Acting Comptroller Milton J. Sokolar about the validity of the figures, he said, "In the final analysis, nobody can absolutely guarantee the accuracy of any figures, but I'd give a lot of weight to GAO figures."

COULD FIGURES in GAO's reports for 1970 through 1978 be off the mark? Sokolar replied with questions of his own: "Is it conceivable? Yes. Is it likely? No."

One top SBA official in a Western state, who asked not to be identified, called SBA's reporting system "simply invalid. What possible good does it do to have some cumulative default rate? What matters is to know what's happened to the loans made in a given year.

"Then we'd have some reasonable idea of the effect of our loaning policies for those years. The way it is now, the only purpose really being served is to conceal what's happening from Congress," he said.

Another top SBA official in a Midwestern state, who also asked not to be identified, said the figures were "not representative of the true picture" but added that there were "obvious reasons" for the SBA's method of reporting the loss rate.

"We've been told to push these great programs, but for every person (who gets a loan) at the end of the pipeline, there are 9,999 who don't like government giveaways." Hence, the figures "are masked for the best possible picture," he said.

NEXT: Successes follow the book

Reprints on sale:
Reprints of this series will be available in booklet form in two to three weeks. Mail orders can be sent to: SBA Reprint, St. Louis Globe-Democrat, 710 N. Tucker Blvd., St. Louis, Mo. 63101. The first copy is $1.25; each additional copy is $1. Checks should be made payable to St. Louis Globe-Democrat.

Success Stories Tell How SBA Should Work

(By Thomas L. Amberg and Michael R. Montgomery)

Successes in the Small Business Administration's direct loan program have come when SBA granted loans to applicants who had experience in the business and general management, and who invested something of value of their own in the enterprise.

Those success stories point clearly to why 42 percent of the loans end in failure and default.

The agency's lax procedures in the last decade have allowed many without experience or managerial ability and with little personal financial stake in the business to avail themselves of huge amounts of federal money at the taxpayers' expense.

The Globe-Democrat asked SBA district offices throughout the country to submit a list of borrowers who had gotten direct loans and done well in business, either paying the loan off entirely or continuing to make regular payments.

After interviewing these "successes," reporters found that, in all but a handful of cases, the reasons for success boiled down to: experience in the business, some general managerial experience, and investment of personal money or equity by the borrower.

The successful firms reviewed by The Glove-Democrat tend to be those that received loans "by the book," that is, with SBA closely following its regulations calling for loans only to those with experience in the business they are seeking to enter, with managerial experience, with "a reasonable amount (of personal equity) at stake in the business" and with an assurance of repayment ability.

The investigation shows those with little business or general managerial experience tend to be the ones who end up in default.

Some examples of the successful businesses:

In 1971, Seymour Beneroff was running a small, "hole in the wall," corrugated package company in Brooklyn, N.Y., when the city forced him out of his building to make room for a building project. Beneroff turned to the SBA for a loan to allow him to buy his own building in Linden, N.J., and the agency complied, making him a loan for $202,500.

Since then business has boomed and Beneroff has about 75 employees, he says. "Without the SBA's help, I don't think we would have gotten anywhere," he says.

Beneroff had several things going for him as well. He had spent 18 years in the corrugated package business, spending much of that time as a sales manager and general manager, before founding his own firm, Squire Corrugated Container Corp., in 1967.

Beneroff has his own ideas about what works at SBA and what does not. "When they try to make it a social program, seeking out special groups to help, it seems to fail. But when they stick to helping young businesses, that's when it really works."

Nunzio J. Incremona was operating a small garden and florist shop in a Philadelphia mart in 1979 and had been doing a brisk business for several years when an SBA loan official happened to take note of the business and asked Incremona whether he would be interested in expanding.

With a $30,000 loan from SBA and $12,000 of his own money, Incremona set up Incremona's West End Florist and Garden Center in Lansdale, Pa., a Philadelphia suburb. Business has increased 150 percent in the last year alone, and he has expanded into a full-scale nursery and greenhouse, he says.

St. Louisan Herschell Clark says his SBA direct loan six years ago "really helped me out." At that time his fledgling firm was undercapitalized and badly in need of money to help it expand, he says. When banks turned him down, he turned to the SBA, which gave him $20,000.

Clark had about eight years experience in tire operations, including managerial experience, before receiving his SBA loan and opening the Clark Tire Co.

Since then, business has "just about doubled every year," and sales this year will exceed $2 million, he says. Whereas he had been renting the building where the firm is located, at 10520 Big Bend Blvd., he has since bought the entire block, opened a second store and is considering a third.

In making the loan, SBA did something it now rarely does—it went out and looked at the business location and did thorough cash flow projections. Clark put up two houses and two cars as collateral.

In addition, SBA did something else it rarely does now—a servicing officer visited Clark every three months or so to check on the business and offer advice. Clark's loan will be paid off in about a year, he says.

Having been a branch manager for the Wurlitzer Co. in Boston for five years, Gene B. Hale Jr. earned a master's degree in business and then ventured into business. Turned down by banks, he won the approval of the SBA for a $66,500 loan in 1977 and set up Hale Piano & Organ Co. in a regional mall store in Madison, N.J.

Since then, the SBA has given him another $88,500 for a second store, and business has been so successful he has been able to open a total of four stores. Sales have more than quadrupled in less than four years, and he has a good relationship with a local bank, enabling him to move out from under the federal government's wing, he says.

Tyree W. Hale has a long history of experience in the mortuary business in St. Louis, having graduated from mortuary school in 1947 and worked in the business ever since. He built Hale Funeral Home in 1962 at 1238 N. Kingshighway Blvd., and got his first SBA loan, for $1,600, in 1964.

Since then, SBA has given him three more loans, totaling $36,000, enabling him to expand his business, and has sent SCORE (Service Corps of Retired Executives) representatives to help him with specific business problems.

He credits SBA with giving him the chance to expand his business, but adds, "SBA isn't in business to put people in a successful business. They're there to help you, but you've got to be able to make it go yourself."

He advises younger people wanting to get a start in business "to get some working knowledge of the business they want to go into" before they seek a loan.

"I spent a year and a half working in insurance just to find out what kind of insurance problems I'd run into in the funeral business," he says.

In virtually every case examined by reporters, successes in the direct loan program involved people entering a business in which they had had past experience, with at least a modest background of management in some type of business, and with a certain amount of their own equity involved.

Mr. HILER. Thank you, Mr. Chairman. I'm glad it wasn't the Globe-Republican in this case. [Laughter.]

Are you familiar with this article?

Mr. TEMPLEMAN. I believe so, yes.

Mr. HILER. I am going to submit it for the record, but I would just like to read a couple of paragraphs and hear your comments on it.

I might say that more than 18,500 records, reflecting 26.8 percent of the Small Business Administration's direct loans made nationwide, from 1970 through 1978, were statistically analyzed with the assistance of Michael Jones of Comshare, Inc. The records were obtained under the Freedom of Information Act, and 18,500 records is a lot of records.

It goes on to say that their figures indicate that the number of loans that were defaulted by an analysis of 26.8 percent of the loans was 42 percent direct loans, and that the total dollars of those loans were 33.3 percent. How do you respond to what I have read and what I have interpolated from the article?

Mr. TEMPLEMAN. Well, basically I would respond in a general fashion first and then get to the 42 percent, if that's all right. Certainly the direct loan program within SBA over the last several years, hopefully up until this last year, has been very mismanaged. There have been quotas, there have been goals, there have been targets to, in effect, get the money out there. I am sure they have helped a lot of people. I personally have talked to people that those loans have hurt.

I would say a minority—and not minority in the racial sense—a minority of the loan applicants get hurt by them, but there are people who really didn't know what they were doing and the SBA people had the obligation to push money out. So there has to be a change, even in this year. With our 1982 funds we have begun to change it. We no longer have the targets in the field, and we no

longer have this need to push money out. We are trying to do it in a proper fashion and in accordance with good lending principles.

The 42 percent is based——

The figure that they come up with, I probably should let Mr. Holloway answer that, but I first want to say that it is misleading because it is based on a default rate rather than on a loss rate.

Mr. HOLLOWAY. Congressman, that study was one of the items that underscored for us the necessity, really, to return, if you will, to the criteria laid down by the Small Business Act, that there be a reasonable assurance of repayment. We believe that is wise counsel, and the need for money cannot really be confused with the need for more debt service or the need for a loan if it cannot be repaid.

To intentionally make these loans and get people in trouble with the Federal Claims Collection Act and all that goes with that is just not intended by any of us. We are trying to look very carefully at the statutory criteria, a reasonable assurance of repayment. That is the policy that we are presently following.

Mr. HILER. I'm confused. You kind of shrug off the 42 percent by saying that it is misleading. If you don't want to talk about the number of loans defaulted, how about the 33.3 percent dollars loss that have been incurred? That's extrapolated from doing 18,500 records at 16 offices across the country.

Mr. TEMPLEMAN. I wasn't meaning to shrug it off. I think Ed can answer that better than I can, is what I was saying, because that is part of his responsibility, the loan servicing area.

Mr. HOLLOWAY. The actual default figure is far different from the loss figure. People get 1 month behind on their payments and they are in default. But there are many loans that are in default on which not $1 of loss is ever experienced.

Mr. HILER. Excuse me for 1 minute for interrupting. If we're saying the 42 percent that are defaulted is not accurate, then how do you respond to the 33.3 percent that they say are losses. I mean, actual dollars that are gone, not defaults that haven't been met this week, but 33 percent that actually have never been repaid, representing $157,535,380 out of $473 million and some odd cents that were loaned at these 16 offices during that 8-year time period.

I guess that's the figure. Are you saying that loss figure is not correct?

Mr. HOLLOWAY. I'm saying, Congressman, that that figure is essentially correct, and that was the frightening part of it. That happened in cities like Detroit and other places, where there was an honest belief and an effort made that making a lot of loans was the solution to many of the problems there.

Mr. HILER. So we're saying $1 in every $3 that was loaned by the Small Business Administration over an 8-year time period was lost?

Mr. HOLLOWAY. In those particular cities, where that St. Louis study was made, which were cities like Detroit and New York and Chicago and other places, that is correct. There were tremendous losses.

Mr. HILER. I guess I become concerned, when we look at 13 million small businesses in the country, and we made direct loans to 5,400 last year, an extraordinarily small percentage of people, and

then you take that extraordinarily small percentage and $1 out of every $3 goes up in flames, I guess I sit and wonder why are we having a direct loan program. I mean, I guess I come to your conclusion that it seems to me we haven't managed it very well in the last 12 years. Sure, we could throw in more money and say we'll do better next year. But I start to wonder, with that incredibly small number of businesses, whether we're doing anybody any favors by going forward with the direct loan program.

Mr. TEMPLEMAN. Of course, that's what we arrived at as well. Also, back to the point of how much manpower it takes. We had roughly 150 people involved in direct loans in fiscal year 1981. As the direct loan program is being reduced, these people were transferred to debt servicing and debt collection. You transfer those same people—they have similar skills—to getting the money back that is legitimately owed.

Mr. HILER. Would some of those people also be going into the guaranteed area, where there might be greater management assistance provided? Or is no transfer going on like that?

Mr. TEMPLEMAN. No; in the guaranteed area, we're actually giving more responsibilities to the banks continually. In terms of the processing, we are basically taking what surplus manpower comes out of that in the demise of the direct loan program and concentrating on debt collections.

Mr. HILER. I will yield back for the time being.

I might just make one comment. Across from my congressional office in South Bend is the Small Business Administration office, right across the hall. We have had, as you might imagine, a number of contacts with the Small Business Administration people there. I would like to say that at no time in the last 14 months has our office ever perceived that there were delaying tactics taking place. So, certainly at the field office level, we have had extremely good cooperation with your people there, and I think you are to be highly commended for that.

I yield back at this time.

Mr. ADDABBO. Thank you.

Having sat on this committee for a few years, and having gone into the question of direct loans and being still a proponent of the direct loan program, we are all startled when we see those figures. But I think it was alluded to by Mr. Templeman that you have to look beyond the figures. You have to look at the benefits the direct loan program has given to many, and you do not use this administration's syndrome of throwing the baby out with the dirty water. If you have bad features within the program, you do not destroy the entire program.

If we look at the record of the hearings of this committee and the investigations of this committee, we will find that much of these losses were due to games played by administrations, both Democratic and Republican administrations. We have taken them both to task when they played the numbers game. That was the reason for those failures, because the President, whether it be Carter or Ford, before them or after them, wanted to go to the small business community and say, "We made 100 loans, we made 1,000 loans." What would happen in those cases—and again, this is all proof positive in the hearings we have had—if a man needed $30,000 to

stay in business, they would say "you can do with $15,000." So they underfinance them right at the beginning and they're behind the 8 ball before they even get started. That was the work of this committee in trying to correct that, so that the administration or the Administrator did not play the numbers game, and the numbers game is what caused those losses.

What we're saying is the program is good, but the administration of it is bad, and what you need is the proper personnel to administer the program so you don't throw out the baby with the dirty water. You clean up the water and you help the small businesses as we directed by law back in the fifties.

The gentleman from Nebraska.

Mr. DAUB. Thank you very much, Mr. Chairman.

There are a number of things I would like to say, and time won't permit me to do all of that, so I want to go right to questions now.

I want to first thank you for coming, and then I want to agree with Mr. Hiler's feelings. I, too, have an office right across the hall in my district office in Nebraska. Our small business folks there and our small business council, some 1,000 small businesses, are most appreciative for the great job that they're doing there. They have been most responsive for as long as I have been in Congress, and I look forward to continuing to operate with them.

Mr. Addabbo, I might point out—I'm sure your staff has for you this December 1981 management information summary that would give you the figures on guaranteed and direct, in fact the combination, from the first quarter of 1981, 9,112 loans. That dollar volume was $1.079 million. A year later, the first quarter of 1982, the number of loans had dropped to 3,542—that's combining direct and guaranteed—and that total dollar volume is $395 million. So about a third across the board in numbers and money. The figures are in the first three pages of the report here.

Mr. ADDABBO. They coincide with the reduction in force by the SBA.

Mr. DAUB. Is that the same percentage, 200 over 4,200?

Mr. ADDABBO. Close to it.

Mr. DAUB. I think it's the economy more than anything else. A very bipartisan statement, if I might. [Laughter.]

Well, the figures I thought you were looking for, you could get them right out of the book. They are there. Second, I want to note that the previous administration had dollar goals and quotas, did they not?

Mr. TEMPLEMAN. They did.

Mr. DAUB. That was a way of forcing money out the door and that way people merit increases. Is that policy still in effect?

Mr. TEMPLEMAN. It is not.

Mr. DAUB. I want to turn to the two subjects that concern me most in this budget. The first one is with respect to the line item in the budget. Can you tell me what figure has been budgeted that accurately pinpoints the amount of recoveries on overdue loans that you expect to make, the assumed figure in the budget?

Mr. TEMPLEMAN. The Office of Management and Budget has given us the goal of collecting $175 million in fiscal year 1983, more than what we have already done; that's an increase.

Mr. DAUB. That's a nice way of answering my question, too. I appreciate that.

If we define a delinquent loan as one on which payments are 60 days overdue?

Mr. TEMPLEMAN. Sixty days or more.

Mr. DAUB. How much of that total portfolio is outstanding and delinquent at this time?

Mr. HOLLOWAY. The amount of all SBA loans—60 days or more delinquent—is 6.36 percent, a little over $1 billion. In numbers, it is 63,024 loans for 12.63 percent that are delinquent 60 days and over.

Mr. DAUB. Say the figure again in dollars?

Mr. HOLLOWAY. In dollars, $1.358 billion, which is 7.88 percent of the total amount outstanding. I'm sorry, Congressman, I was reading another figure.

The delinquent amount is $1.097 billion, or 6.36 percent.

Mr. DAUB. OK. Now, follow that, if you will, by a comment with respect to liquidations.

Mr. HOLLOWAY. In liquidations, the total number in liquidation is 21,604——

Mr. DAUB. What's the definition to move to liquidation?

Mr. HOLLOWAY. An account is classified in liquidation when the judgment is made that we can no longer do anything to help the small businessman survive, but we must now move to protect the interests of the Government.

Mr. DAUB. So we're talking about 21,604 loans in liquidation?

Mr. HOLLOWAY. In liquidation, yes, sir.

Mr. DAUB. We're talking about 63,000 loans that are 60 days or more past due?

Mr. HOLLOWAY. Yes, sir.

Mr. DAUB. That's 63,000 individual loans?

Mr. HOLLOWAY. Yes, sir.

Mr. DAUB. How much of the delinquent portfolio is collectable at this time? I'll say it differently. What portion of the loans that are delinquent are now payable, and what portion are not yet due according to their payment schedule?

Mr. HOLLOWAY. I would answer by saying that, in terms of our recordkeeping, anything that is delinquent and not classified in liquidation, we expect to collect that money.

The loans that are in liquidation, we know from experience, we will collect half of them, or about 47 to 50 percent. That's over the past 3 years. This is the recovery rate.

Mr. DAUB. Forty-eight cents on the dollar would be closer?

Mr. HOLLOWAY. Yes, sir.

Mr. DAUB. Is this recovery ratio taken into account in the budget assumption for debt collection, in other words the $175 million we're talking about?

Mr. TEMPLEMAN. Yes.

Mr. DAUB. That doesn't seem to add up. How do you figure it, then? Shouldn't you be collecting a lot more than $175 million?

Mr. HOLLOWAY. That's 175 more than was collected last year, which is over $1 billion.

Mr. DAUB. A billion dollars?

Mr. HOLLOWAY. Over $1 billion; $1.2 billion.

Mr. DAUB. What happens if you don't meet the target of collecting as much as you hope to collect? What happens to the budget if you don't collect that money? Has anybody ever thought about that?

Mr. HOLLOWAY. Yes, sir.

Mr. DAUB. Where do you get that money?

Mr. HOLLOWAY. It may be necessary under those circumstances for us to either curtail programs or to seek a supplemental appropriation.

Mr. TEMPLEMAN. Yes, it's true, the budget is based on collecting that money. If it doesn't come in, we have to look at other sources.

Mr. DAUB. Ah, you're just really driving some of us up a tree when you say that. You know because that's even tougher to do than dealing with the reality—and I think much of this budget is reality. That is one I want you to go back and look at, because I think in this economic "dish" that we're in—the bottom of the dish now—I do not see you doing $175 million better than you did last year. I would hope you could hold your own in terms of getting cash in on what are already classified as delinquent or even liquidated types of loans.

I understand the intention. I think your enforcement procedures are much better now than they were a year ago. I know you have beefed that up and you're making a dedicated effort. This committee appreciates, I know, the fact that our programs can be maligned by articles like my colleague just put into the record, when statistical history builds up over 8 years and we've got an organization in our Government that allowed that mismanagement to occur. You shouldn't have to bear the burden in total for the ills of the past.

But I do believe that that figure is tough to expect. As a result, Mr. Chairman, I think that leaves us, as a committee, in a difficult position. We have to go to other committees of Congress and to the floor on whatever figures we arrive at here and say, you know, we're going to be OK for the year. So I would like you to take a look at that and maybe test OMB's consideration of that figure. It may be the one figure in this whole budget that I think throws you off over this next year.

Mr. TEMPLEMAN. We would be glad to.

Mr. DAUB. Now, I have one other point and then I'm through, Mr. Chairman.

I am concerned about the Small Business Investment Company situation. MESBICs are funded, Mr. Chairman, if I remember correctly, but the regular SBICs are not. Can you say for the record again why that determination has been made?

Mr. HOLLOWAY. Well, we are funding the investment company program to the extent of $125 million, as well as $41 million of direct money for MESBICs.

Mr. DAUB. But aren't you talking about relying upon sort of the pay off of debentures in what might be a float?

Mr. HOLLOWAY. There is a question as to how much of the presently maturing portfolio will have to be refunded. We believe, from our analysis, that of the maturing obligations we will be able, on a reasonable basis, to accommodate the ones that should be rolled over and refunded.

Mr. DAUB. On a 10-year basis?

Mr. HOLLOWAY. On an appropriate basis, based on the credit of that individual case.

Mr. DAUB. The ones that go bad?

Mr. HOLLOWAY. A great many of those with maturing obligations for this next year are in liquidation, so there certainly won't be a question of refunding those.

Mr. DAUB. What about new money? I mean, absolutely brand new money to start new small business investment companies?

Mr. HOLLOWAY. There won't be a lot of new money for that purpose. However, it may be that a number of the obligations coming due will be paid. There is really no obligation when these debentures are purchased that they will remain outstanding forever and always be rolled over.

Mr. MITCHELL [presiding]. Would you yield for a moment on that point?

Mr. DAUB. But we owe somebody that money. It doesn't stay with us. It comes into the liquidation and we have to pay off to the holder of the financing instrument, right?

Mr. HOLLOWAY. As long as the——

Mr. DAUB. The Government doesn't get a windfall. We don't have any new money from that transaction to loan out to the next new small business investment company.

Mr. HOLLOWAY. No, sir.

Mr. DAUB. So what I'm looking for—and I would be happy to yield to the chairman—is that if we're talking about supply side, and if we're talking about "New Federalism," if we're talking about private sector and the multiplier effect of this kind of a loan, isn't this much more in line with what we ought to be doing with our money, putting another $100 million into this program?

Mr. MITCHELL. If the gentleman will yield——

Mr. DAUB. Yes, I will, Mr. Chairman.

Mr. MITCHELL. Because you're on a point that is of great significance to me. Not only is there no request for new money, but apparently SBA is expending in SBICs less than two-thirds of the appropriated level.

It's a simple matter of record, Mr. Daub, that in December through February SBICs requested $71-plus million in guarantees, but only $28 to $29 million was disbursed. The demand is there, that's what I'm saying.

Mr. DAUB. I would think, especially in times like these, when you can make a little available for private sector contributions, and in turn they can stage that or tier it in—— What's a fair figure, $2 million can start a pretty viable SBIC?

Mr. TEMPLEMAN. Yes, sir.

Mr. DAUB. That could layer itself into who knows what in terms of jobs and taxpayers and all the rest.

I guess I would again like you to go back and take a look, as you shift some thinking, either in your own shop or in OMB. Mr. Chairman, I don't want to grill them on it, but I would like them to know how I, and maybe others on the committee, feel.

I appreciate the time and thank you again for coming here.

Mr. MITCHELL. Thank you very much.

Mr. Staton is next.

Mr. STATON. Mr. Templeman, are you going to be glad when Mr. Sanders gets confirmed? [Laughter.]

Mr. TEMPLEMAN. I've had that feeling a time or two even before today. Well, I appreciate your being here.

Mr. STATON. I happened to read an article in Time magazine a few issues ago which stated something along the line that the Fortune top 1,000 companies had, as far as employment is concerned, virtually no growth. In fact, they probably declined in the number of jobs that they provide, while during the same time period—and I don't recall the exact time period—small businesses created over 3 million new jobs. Further, to respond to my colleague from Nebraska, as far as venture capital is concerned, there is about 100 times the volume of venture capital that was available in the marketplace only 6 years ago. So there is a feeling that money is available and the thing that is holding it down, as I understand from your earlier testimony here, is the interest rates.

I just returned, of course, as many of us did, from having spent a week in my district and talking to small businesses. I would like to ask what your feeling is regarding an interest rate which you feel entrepreneurial people are willing to take a little bit more of a risk than the safe bet mentality that seems to plague the Fortune top 1,000 companies? Small businessmen are, by and large, gamblers.

What decline do you see we are going to have to reach in the next 60 to 90 days to stimulate the growth, which obviously there is venture capital there.

Mr. TEMPLEMAN. There is, as you say, more venture capital than there has been for years. The reaction to interest rates, I believe, are made up of several components, one of which is purely psychological.

A few months ago or a year ago a 12 percent interest rate was considered extremely high. Of course, we have been all the way up to 21 in 1980 and we're at 16½ now. Whether the risk pays or whether the venture pays in relation to the risk in the interest rate, probably is—this is an intuitive feeling—in the 11 to 12 percent range over a period of time. I think the small business entrepreneur, who is a gambler, but a very clever and a very smart one quite often, is not only looking at the interest rate that is high, but the fact that it goes up and down. It's the fluctuation, the uncertainty.

Whenever we reach for some period of time, a few months, at least, around the 12 percent range, I think that will move not only entrepreneurs but even the housing industry.

Mr. STATON. Since we're among friends here, do you have a private feeling regarding actions that this committee could recommend to the Congress that would bring about a more swift reduction in the interest rates?

Mr. TEMPLEMAN. I believe there is a real valid base to the idea of getting the Government out of the capital market. In the recent period the Government took for its own purposes 43 percent of all the capital that was raised in the private market. Obviously, with that, plus the deficit of something in the neighborhood of $100 billion, the people that make these decisions in the thousands of financial institutions are gun-shy, pure and simple.

I recognize, as the chairman has said, that the loan guarantee portion of the Small Business Administration is very small in terms of other things. But I think we collectively have got to get the Government out of the financial markets, and that will begin to stabilize the interest rate and make an accessible risk valid.

Mr. STATON. I don't believe that the money budgeted in the SBA budget for direct or guaranteed loans is a destimulating factor. We had an article in our hometown newspaper just a couple of weeks ago in which our local SBA people were saying, virtually advertising the fact, that we have money to loan and no applicants. It isn't, to me, a problem of underfunding the program as much as it is a problem of, again as you pointed out, reaching a position of stabilizing the economy as it relates to interest rates. I have been pleased with the outreach that we have seen from the SBA offices making this kind of a pitch for small businesses to generate some work.

I have a couple of questions regarding policy, and one of them that concerns me is the unilateral decision on the part of OMB to disapprove any pollution control bonds which are planned as tax exempt. Could you give us what the policy rationale for that might have been?

Mr. TEMPLEMAN. Well, again the feeling is, on their part, that this was another intervention of the Government in the private capital sector. I would say, of course, that if the Congress has the final word, OMB has proposed a reduction, that Mr. Smith of the Appropriations Committee, after we had notified—you know, in accordance with the way we are required to do—has come back and said "no way." We are expecting a similar letter from the Senate and we will be going back to OMB. Congress will have the final word here.

Mr. STATON. That's comforting.

I again would just like to echo some thoughts of the gentleman from Indiana here, that is that 5,400 direct loans out of 13 million small businesses is really an abysmally small percentage to directly affect. We wonder if the amount of money allocated for staffing, for collection, for making the loan to begin with, isn't that a part of what is holding up the interest rates for all the remaining 13 million people in small business who are trying to get rates down and capital available to them? We aren't really affecting enough of a number, that it really does stimulate the economy to any great degree.

I also am concerned that we're taking in some respects the risk and the concern out of someone who is vitally interested in a business. It would seem to me, if we look back over the history of our country, that we would suspect that small business helped Thomas Edison and people like this, that had there not been a Small Business Administration perhaps we wouldn't have the light bulb; that's nonsense.

We had people who had a saleable idea and who believed in their idea enough that they were able to go out and sell that idea to their backers and to take a risk. It seems to me like we're moving toward an area where we want a no-risk situation. The small businessman forms a corporation and to protect against the future loss, perhaps, he wants a guaranteed loan to protect the default. We join in this with the hope that it will stimulate small business growth,

but it seems to me it has had the reverse effect, and that what we have is venture capital available for those who are willing to take a risk and if their idea is saleable enough they will, indeed, do so. The only thing we're waiting on right now is not more money in the Small Business Administration for direct or guaranteed loans, but it is for our interest rates to stabilize and reach a point where the risk for the return is worth the risk.

I would ask you along that line, after I have made my little speech there, what we are going to do for increasing private sector participation in the management assistance, which I think is a definite goal that SBA should undertake.

Mr. TEMPLEMAN. We have begun a private sector outreach effort in management assistance. We are involving groups that had not formerly——

Mr. STATON. Is this like the SCORE?

Mr. TEMPLEMAN. SCORE. Well, I am kind of categorizing the assistance in two groups, ones that had not worked before, and then I would like to speak about SCORE and SBDC's and small business institutes and that type of thing.

But we are going beyond what we used before. We are getting groups of accountants, trade associations, private individuals that are willing to devote some of their time. We signed an agreement with a CPA organization in California to devote 10 percent of their designated individuals time to small business for no charge. The biggest problem, of course, in small business is knowing how to keep the books and being able to meet all the requirements.

We are reaching out in an organized way to reach new sources of private sector involvement. At the same time, we are improving the SCORE program. We have 8,000 to 10,000 people signed up that theoretically are in the program. Not all of them have worked in the program to any significant amount. Not all of them are up to date. Some of these individuals, of course, are retired. They have been away from their trades and whatnot for several years, and things change rapidly, especially technologies.

Also, the majority of those people are from large business firms, and they have to have some training how to relate to small business. So we are improving SCORE.

The SBDC effort, even with the reduced level that we have proposed will maintain all of the current SBDC's. In fact, we have a few cases where the States can't raise the money to match with ours. Some places will not be able to use all of the money that we can allocate to certain SBDC's. Furthermore, we are improving the SBDC administration. We have made a couple of changes in schools in order to get better administration.

We strongly support the Small Business Institutes where the graduate students go out and help small businesses. We are working with the junior colleges. We are working with chambers of commerce. We are reaching out wherever we can to find people that are willing to help, sometimes partially supported by us.

We believe the Federal Government must reduce its size. We couldn't afford to hire all the business counselors we needed, if we could get them. Second, business people can counsel business people better than civil servants. I don't mean that in a derogatory manner, but they are in business.

So we are reaching out on a broad spectrum to get better and more counseling. Even with these reduced personnel levels, with a coordination function rather than a counseling function, we will have more management assistance.

Mr. STATON. Thank you very much. No further questions, Mr. Chairman.

Mr. MITCHELL. Thank you.

I have one or two questions. First of all, let me go back to this reduction in force of 220 people. Where did this originate? Did it originate from within SBA?

Mr. TEMPLEMAN. The entire nondefense part of the Government was affected by the President's plan to reduce Federal personnel. I believe the figure you said over that many fiscal years was 75,000.

Mr. MITCHELL. 75,000.

Mr. TEMPLEMAN. It is the entire portion of that.

Mr. MITCHELL. So it originated within SBA?

Mr. TEMPLEMAN. No, sir; it came from the President.

Mr. MITCHELL. From the President; all right.

The second question is on the pollution bond guarantees program. When Congress passed this program, there was an absolute consensus that these bonds ought to have tax-exempt status, that the program wouldn't work unless that was there. It is my impression that the Small Business Administration has been arbitrarily refusing to approve guarantees on tax exempts. Is that an incorrect impression?

Mr. TEMPLEMAN. Ed, would you speak to that? He has got more of the detail on that than I have.

Mr. HOLLOWAY. Mr. Chairman, the President originally proposed to cut the pollution control bond program from $250 million to $50 million.

Mr. MITCHELL. Yes.

Mr. HOLLOWAY. We went back with an appeal on that, and the agreement that was ultimately reached was that $150 million would be the request amount, but they would restrict us from doing tax exempt deals.

Now, the policy of the administration, as a part of reducing Government intervention in the credit markets has been to discourage tax exempt transactions. Apparently, the law says they may be tax exempt and it does not say that they will, in a mandatory sense, be tax exempt.

Mr. MITCHELL. If I may interrupt you, I think that is one of the things that the committee will have to correct.

Mr. HOLLOWAY. Yes, sir.

Mr. MITCHELL. Because it was made absolutely clear during the discussion on the pollution bond guarantees program that it wouldn't work unless the bonds had tax-exempt status. In that connection, you returned $94 million in guaranteed applications and told them to revise and resubmit as nontax-exempt, right?

Mr. HOLLOWAY. Yes, sir.

Mr. MITCHELL. How many have been resubmitted?

Mr. HOLLOWAY. Only a small amount so far; I would say four or five. We are just beginning to get responses to the letters that we sent out. We expect a fairly reasonable number to want to pursue the matter on a taxable basis, as opposed to no assistance at all.

Mr. MITCHELL. My problem is: How do you define a fairly reasonable number? I am assuming that you aren't going to get anywhere near the number of applications resubmitted as has been originally.

Mr. HOLLOWAY. What we are talking about, essentially, is a difference of anywhere from probably 2 to 5 percent of interest rate, the difference between the taxable and nontaxable.

Mr. MITCHELL. Yes.

Mr. HOLLOWAY. So, in the case of those businesses where to pay an extra 2 to 5 percent, the credit does not add up. Then, if it doesn't make sense for them, they won't do it?

Mr. MITCHELL. Given the margins where guys are operating right now, that 2 to 5 percent could kill them.

Mr. HOLLOWAY. Yes, sir.

Mr. MITCHELL. So I would like for the staff to make a note that we do need to look at the legislation and attempt to make it mandatory.

Let me ask you a little bit about your bank certification program. That was designed to assist in expediting loan processing in banks whose priority was to offer SBA clients guaranteed loans. That is the certification program.

Mr. HOLLOWAY. Yes.

Mr. MITCHELL. How many banks now participate in your bank certification program?

Mr. HOLLOWAY. Just over 500.

Mr. TEMPLEMAN. Just over 500.

Mr. MITCHELL. What would you expect a reasonable participation rate to be?

Mr. HOLLOWAY. This year, I would think in terms of an extra 100 to 150 additional banks coming in that program.

Mr. MITCHELL. That might make it as much as 700.

Mr. HOLLOWAY. As much as 600 to 700.

Mr. MITCHELL. Theoretically, what would your desirable objective be on the participation?

Mr. HOLLOWAY. Well, we have a total of about 11,000 banks that have at least one SBA loan in their portfolio. We have about 600 banks that do a very active business with SBA. So, if 600 banks are very active, ultimately there could be 800, or as high as 1,000 that would be doing enough business with us to fall into the routine of operating in an accelerated manner.

Mr. MITCHELL. We have an enormous persisting problem about minority loans with the banks. You are aware of that. That is one of the reasons why I am so strong on retaining direct-loan money. In your bank certification program, how many of those 500 banks have made minority loans; do you know?

Mr. HOLLOWAY. Congressman, I believe that all of those banks are making some minority loans. I don't have the exact figure.

Mr. MITCHELL. This is one of your favorite programs, and it is a desirable one. I would want you to take a looksee at the loans made by the banks that are in your bank certification program, break them down for minorities and nonminorities.

Mr. HOLLOWAY. I can get that information for you. We will get that.

Mr. MITCHELL. Unless some miracle has taken place, you are going to see an enormous discrepancy between the lending practices to minorities and nonminorities, and that is with your best banks.

[The information follows:]

In the bank certification program, for the period of October 1, 1981 through December 31, 1981, we have made a total of 498 loans for $61.3 million.

Of that amount, 48 loans for $5.3 million have been made to minority borrowers. This is approximately 10 percent of the number of loans, and 8.6 percent of the dollars. This follows quite closely our experience in overall guaranty lending which at January 31, 1982 stands at 10.9 percent of the number, and 8.7 percent of the dollars.

Mr. MITCHELL. Further questions?

Mr. HILER. Yes. Thank you, Mr. Chairman.

Just a couple other points. I also would like to speak to the SBIC financing. I think that that is something that we will want to look very closely at. When one looks at the list of companies that have utilized SBIC financing over the years, one comes up with really a remarkable set of companies. Some of the success stories are: Memorex, which has alternated between success and failure, but, all the same, is a very large company; Federal Express, which most people have acknowledged to be one of the really, probably the preeminent example of venture capital and risk bearing on the part of a group of people to make it a tremendously successful company; Teledyne has been a tremendous example of several people who have put together, once again, a tremendous company; also Time Share; Storage Technology; Four Phase; Amdahl, Advanced Micro Devices are all extremely successful companies.

I am sure there are failures along the way, but I would suggest that the successes probably far outweigh the failures when you look at the entire history of the program.

I might also just touch for a minute on the pollution guarantee part of the portfolio. What was the 1980 appropriation in that area?

Mr. HOLLOWAY. 1980?

Mr. HILER. Do you have that?

Mr. HOLLOWAY. We did $98.5 million in 1980.

Mr. HILER. OK. In 1981?

Mr. HOLLOWAY. $100 million?

Mr. HILER. Projected for 1982?

Mr. HOLLOWAY. For 1982, our revised number is $150 million; $50 million tax exempt, $100 million taxable.

Mr. HILER. OK. In 1981, was that all tax exempt?

Mr. HOLLOWAY. Yes, sir, it was all tax exempt in 1980 and 1981.

Mr. HILER. Now in 1983 the proposal is $150 million?

Mr. HOLLOWAY. $150 million.

Mr. HILER. That would all be taxable?

Mr. HOLLOWAY. That would all be taxable.

Mr. HILER. So the key issue here is probably not going to be so much the level as whether it is tax exempt or taxable.

Mr. Chairman, I have no further questions.

Mr. MITCHELL. Thank you. I have just one or two more that I will ask now, and about 15 that I am going to submit to you in writing for response.

Mr. Staton is gone, but he touched on a problem that is exceedingly difficult. He says that in his neck of the woods SBA is saying, "Come on in, we have got money to loan." In my city, I am being banged on every day by people who have been to SBA and are told, "We have no money."

Isn't there some kind of arrangement that can be worked out where, after a certain period of time, if in one region or one area the money is not being spent, it can be transferred to an area of need? Is that unrealistic?

Mr. TEMPLEMAN. No, not at all. Mr. Chairman, we have just in the last few days put out direction to our field that—and I could submit a copy of that direction for the record if you would like—whenever the region is coming up against their so-called allocation in the guaranteed program, handicapped loans, energy, 503, whatever, their budget officer simply needs to pick up the phone and call Washington and we will allocate money that is not being used somewhere else. We make allocations normally on a quarterly basis, but it is a totally flexible system.

[Memorandum referred to above follows:]

SBA Washington, DC 20416 **Memorandum**

Date: FEB 19 1982

From: Edwin T. Holloway, Acting AA/FI

Subject: Allocation of Additional Loan Funds

To: All Regional Administrators
All District Directors
All Regional Budget Officers

It is recognized that loan demand at this time varies considerably from region to region and from district to district.

The purpose of this memorandum is to advise any field office that is experiencing a shortage of loan funds of any type, direct or guaranty, 7(a) or other, including HAL, Energy, and 503, to request additional funds through their Regional Budget Officer.

This memo is not intended to force the usage of funds in cases which do not meet established Agency lending criteria, but to assure that qualified applicants are not denied at the same time that funds are available and unused in another location.

Edwin T. Holloway
Acting Associate Administrator
for Finance and Investment

Field Management OIP

Mr. MITCHELL. That makes good sense, because there is no reason for money to be sitting idle some place in one region, when there is a dire need for it in another place.

In your minority small business capital ownership development program, the salaries and expenses were budgeted at $12.4 million, and that included 370 people and staff. In your 1983 budget, you are proposing a reduction of almost $1 million, and you are also proposing to reduce the staff by 43. That is almost one-fourth of your total staff lost of the 170, almost one-fourth is coming out of the minority small business capital ownership development. What exactly is being cut when you propose a reduction of $1 million? What functions are being done there that won't be done next year if this goes through?

Mr. TEMPLEMAN. I believe that all of the functions will be done. Before I answer that completely, I would point out that some of the other programs had taken a cut in 1982 and this one did not. It does look as if the cut is greater in 1983 for that program.

Mr. MITCHELL. It certainly does when you look at one small component absorbing one-fourth of the personnel cuts.

Mr. TEMPLEMAN. As far as functions being cut, I don't believe that any functions will be cut. We have, as you know, done a lot of work on that program. We are doing a lot of training, a lot of managing. We have reached the point in all but a couple of cities where we can lift the moratorium on 8(a) applications, including D.C. which we will lift in the middle of next month. They are reallocating people within the program. We basically believe that, with these improvements, service will improve.

Mr. MITCHELL. Mr. Hiler and our staff for some time has been looking at the SBDC operations and getting our own reports together on those. I must say that some of them are excellent; others are not excellent. I hope we can make that a full staff report to the committee.

I have some concern about how many of these institutions can continue to match funding as is being suggested, but we will pursue that after the staff report is submitted.

If you will take my list of questions and respond to them, I would appreciate a very prompt response.

Mr. MITCHELL. Thank you for being here.

Mr. Hiler?

Mr. HILER. Mr. Chairman, I have some questions that I would also like to submit to Mr. Templeman for the record.

Mr. MITCHELL. Let me ask unanimous consent that all the members of the committee may have the right to submit additional questions.

Thank you. It has been an interesting session; I will not waiver from my original position. In fact, the testimony here today that you presented to me has simply buttressed my original position. I think this is an outrageous budget submission, outrageous; the projections are totally off.

The line of inquiry pursued by Mr. Daub points out the illusion that is found in this budget. Again, I just think it is ridiculous to come before a committee of the Congress with projections that you know simply cannot work. You are not going to get another $175 million above what you did last year in collection of delinquent

loans. Threaded throughout your budget request are those absolutely faulty projections. The direct loan cut, I think, is outrageous.

It is our job, as a committee of the Congress, to come up with a budget that is not outrageous. I now call upon each and every member of this committee to join me in helping to fashion a budget based upon real projections, that is going to be fair and equitable and just to all the people who are participants in this program.

Thank you very much for being here gentlemen.

[Whereupon, at 3:12 p.m., the subcommittee adjourned, to reconvene subject to call of the Chair.]

[The following information was received for insertion into the hearing record:]

ADDITIONAL RESPONSES TO CHAIRMAN MITCHELL'S
QUESTIONS ON THE FISCAL YEAR 1983
CONGRESSIONAL BUDGET SUBMISSION

Direct Loans

In 1981 you allowed more than $33 million to lapse in direct loans. In the first quarter this year, you approved $31 million of the $56 million available.

In response to Committee questions as to why you are not using available money, you attribute the low usage to high interest rates and the economy.

QUESTION 1: What is wrong with handicapped loans? Are you trying to tell us that there is only an annualized demand for $9.3 million of the $15 million appropriated for loans at 3 percent?

ANSWER: We cannot state with certainty why the demand for direct handicapped loans has fallen off so sharply. It is possible that general economic conditions have caused potential handicapped applicants to defer borrowing just as have other applicants.

To make sure that funds are available to all qualified applicants that need them we have recently advised all field offices to request any additional funds needed through their regional budget officers so that we may redistribute remaining funds.

Guaranteed Loans

In SBIC guarantees, you are spending at less than two-thirds of the appropriated level. At the same time, you have refused requests for funding. For example, in December of 1981 through February of 1982, SBICs requested guarantees of $71,210,000 but SBA only approved $29,790,000.

QUESTION 1: Why?

ANSWER: The following table provides a summary of SBIC funding activity for the months of December 1981, January 1982, and February 1982.

	Dollar Amount
Total Applications	$ 74,260,000
Denials for Credit or Regulatory Cause	(20,560,000)
Sub-total Eligible SBIC Demand	$ 53,700,000
SBA Approvals and Guarantee	(31,240,000)
Unfunded Eligible SBIC Demand	$ 22,460,000

There are two explanations for the amount of unfunded eligible demand. First, we feel that the amount of applications has been inflated due to the uncertainties in the current year budget process, and the proposals for further budget reduction next year. There is a natural tendency toward excess demand whenever there is a real shortage, or the threat of shortage in any commodity, including, in the present case, SBIC leverage.

Secondly, SBA has been carefully managing the utilization of existing guarantee authority in anticipation of the requirement in the second half of the fiscal year to refund approximately $45.0 million of maturing SBIC leverage. We have administratively earmarked that amount out of the $160 million budget for refunding so that ample authority will be available to comfortably accommodate refunding requests when they arise.

We are attempting in the interim to prorate the non-earmarked portion of $115 million evenly over the year and are just about on target. For the first five months, SBIC leverage has totaled $42.7 million, or an annual rate of $102.5 million, only 11 percent behind target.

We anticipate making up any shortfall in the final quarter (as we did last year under similar circumstances) when the major refundings are behind us.

You are proposing increases in EOL guarantees, and yet you have never used existing authority. In order to approve $100 million in EOL guarantees this year, you would have to increase your performance in the first four months of this year by 1,700 percent in the last eight months.

QUESTION 2: What are you doing to accomplish any increase, much less one of this magnitude?

ANSWER: The Agency will make every effort to make lenders aware of the availability of funds in the EOL program and to encourage the use of the program. However, it is not our intention to artificially achieve a high level of such loan approvals merely for the appearance of achievement. If the demand for the program is there, the funds will be available to meet that demand.

QUESTION 3: Total loan guarantees are off more than 50 percent of program level. High interest rates and the economy may account for some of this.

How much is due to your "tightening" of credit reviews and just what instructions have been sent to the field to implement this policy?

ANSWER: We do not think "tightening" of credit is a totally accurate term. What we have done is to redirect our staff to recognize the statutory requirement for reasonable assurance of repayment.

The adverse effects of granting loans in cases where a reasonable chance for success does not exist, is obviously a disservice to the borrower. We believe this has had some effect on the volume of loan approvals. However, we are unable to clearly identify how much of the drop off has been caused by this as opposed to economic conditions and interest rates. It is our belief, since even non-SBA loan demand has fallen significantly, that the economy is the principal reason for the drop off.

Improved Recoveries and Repurchases

It is our understanding that the budget request assumes that SBA will improve recoveries on loans in liquidation by $100 million in 1982 and by $175 million in 1983.

Question 1: How much is attributable to each revolving fund each year?

ANSWER:

	($ in millions) 1982	1983
Business Loan & Investment Fund	$ 35	$110
Disaster Loan Fund	65	65
Total	$100	$175

Question 2: How much of 1982 projected increase has been achieved to date?

Answer: For the Business Loan and Investment Fund, the actual repayments thru January, 1982 are $73.2 million. Based on this figure, it is anticipated that the total repayments for 1982 will be approximately $244 million. This represents a shortfall of $53.7 million from the amount contained in the budget.

For the Disaster Loan Fund, the actual repayments thru January, 1982 are $246.1 million. Based on this figure, it is anticipated that the total repayments for 1982

will be approximately $648 million. This represents a shortfall of $40 million from the amount contained in the budget. Therefore, it is currently estimated that we will experience a short fall of approximately $94 million this Fiscal Year.

QUESTION 3: Specify the procedures being undertaken to implement this improvement, including a comparison of man-years of effort in 1982 and 1983 vs 1980 and 1981.

ANSWER: See Attachment I.

QUESTION 4: Indicate by revolving fund, the amount in liquidation, and the amount recovered in each of Fiscal years 1978-1981 and corresponding projections for each of 1982 and 1983, both before and after the "improvement" decision.

ANSWER: As of January 31, 1982, disaster loans of all types classified as "In Liquidation" are valued at $231.8 million. There are 6,490 individual cases involved. In the business loan category $1.16 billion is classified "In Liquidation." There are 15,665 loans involved. This latter category includes loans which have resulted from appropriated direct funds as well as loans purchased from banks under the terms of our guaranty agreement. We are making a careful but concerted effort to have banks handle loan liquidations in order to leverage our existing human resources. Of the business loan totals mentioned above, banks are handling 2,973 of them on loan totals of $291.9 million.

From the category "In Liquidation," which we have separately tracked and calculated since the beginning of FY 1979, recoveries were:

1979	$ 129.4 million
1980	139.3 million
1981	155.9 million

We are projecting collections from the "In Liquidation" category as follows:

1982	$ 175 million
1983	$ 200 million

Surety Bonds

In a January 15, 1982 memo to the field, the Administrator said "budgetary considerations have again necessitated a review of the SBG (surety bond guarantee) program levels and a

restatement of underwriting requirements which have a direct effect on those levels".

The Agency then proceeded to limit bonds to $250,000 or one-fourth of the statutory maximum. According to your response to Committee questions, this arbitrary limit will preclude small business from obtaining bonds on some 1,250 contracts. This in turn will preclude them from bidding.

QUESTION 1: Why deny them the ability to participate in the procurement process?

ANSWER: The cutback was part of the President's overall initiative to reduce Federal program outlays and governmen competition in the private financial markets. The $25 000 limit was chosen as the most logical brea point based on previous underwriting experience which indicated that 93 percent of the contracts guaranteed were at or below this amount, with the average presently at about $95,000 per contract. Further, it was felt that the larger contracts would be the best candidates for surety bonding without a government guarantee.

The same memo limits bonds to an increase of 25 percent over previous successfully completed jobs. This again will preclude contractors from even bidding on larger projects.

QUESTION 2: How many will be denied the ability to bid due to this limitation?

ANSWER: Based on monitoring of field activity since the January 15, 1982 memo, the 125 percent limit appears to be having a greater effect than the dollar amount limitation. Because of a reported reduction in contracts advertised for bid and severe weather conditions in many parts of the Nation which have reduced demand for surety bonds, we cannot tell how many contractors have been denied bonds because of this limitation. Since demand is unquestionably lower, SBA is at the moment considering the relaxation of that guideline.

QUESTION 3: Since your activity to date this year would annualize at $816 million as compared to the Congressionally approved level of $1.2 billion, why do "budgetary considerations" necessitate these restrictions?

ANSWER: The lower demand level is hindsight and appears to be based more on general business conditions,

including severe winter weather, than on SBA's revised guidelines. As indicated elsewhere some relaxation of these guidelines is under consideration, but their total removal would create chaos if overall demand returns to normal.

In response to the Committee's question as to your anticipated demand for bond guarantees, you told us that the average annual demand in the past five years has been $1.27 billion per year. This is one of the most nonresponsive "answers" I have ever heard.

Your own approval levels show an increase every year except last year when a budget cap was imposed.

I do not believe that you don't have a demand projection. However, even your figures would indicate that a budget level of $1.08 billion is $200 million less than the average and this precludes some 2,600 bonds per year.

QUESTION 4: How can you justify denying 2,600 small businesses the ability to obtain Federal contracts because they cannot obtain a surety bond as required by Federal law?

ANSWER: While $1.08 billion is nearly $200 million lower than the average demand, we believe the number of contracts involved will be 1200 or less but in the middle to upper volume range. We are in the process of clarifying our guidelines to permit co-insurance and reinsurance agreements above SBA's exposure limit. This should further reduce the number of contracts denied and facilitate more private sector risk on the larger contracts.

Pollution Bonds

When Congress enacted the pollution bond guarantee program, everyone recognized that "tax exempt" status was absolutely necessary to the success of the program. You have now arbitrarily refused to approve guarantees on tax exempts. In answer to a Committee question, you indicated that you returned some $93.5 million in guarantee applications and told the applicants to revise and resubmit as non-tax exempts. You also told the Committee that some have resubmitted.

QUESTION 1: How many have resubmitted?

ANSWER: 32 as of March 2, 1982.

QUESTION 2: How many of the $93.5 million previously submitted and $210 million being prepared, or some $300 million, do you expect to be submitted?

ANSWER: We are uncertain because many potential applicants are waiting to see if tax-exempt financing will be restored, and we have yet to receive responses from 80 of the pending applicants. We also believe much of the demand reflected by the applications received and being prepared as of November, 1981, was in expectation of lower interest rates than are now available on either a taxable or tax-exempt basis.

QUESTION 3: Was this change your idea or was it dictated by OMB

ANSWER: The Office of Management and Budget proposed $50 million of tax-exempt authority for this program in FY 1982. At that time, SBA recognized that this was inadequate against scheduled tax exempt bond closings totalling $40 million and compared to $100 million of financings actually guaranteed during FY 1981. SBA appealed to Office of Management and Budget for an additional $100 million of guaranty authority, and OMB agreed, with the stipulation that no tax-exempt financing be guaranteed after December 31, 1981.

SBA Personnel

Under the Small Business Act, the Administrator is established at Executive Level III, the Deputy at Executive Level IV, the Advocate at Executive Level IV, and Associate Administrators at Executive Level V.

The budget appendix shows one each: Executive III, IV, and V.

QUESTION 1: Who serves as what level and why the discrepancy?

ANSWER: Currently, the Small Business Administration has three Executive Level positions. They are as follows:

Executive III - Administrator
Executive IV - Chief Counsel for Advocacy
Executive V - Inspector General

These three positions required Senate confirmation. All Executive Level IV and V positions that did not require Senate confirmation were changed to SES positions by the Civil Service Reform Act.

QUESTION 2: How many SES personnel slots does SBA have? Submit names, titles and designations as career or other.

ANSWER: The Small Business Administration has 53 SES personnel slots of which 44 are filled and nine are vacant.

The following list reflects those 53 positions:

POSITION TITLE	NAME	APPOINTMENT LEVEL	APPOINTMENT STATUS
Deputy Administrator	Templeman, Donald R.	6	Noncareer
Assoc. Deputy Admin.	Turnbull, Robert A.	5	Noncareer
Deputy General Counsel for General Law	Young, Donald P.	4	Career
Assoc. General Counsel for General Law	Farrell, Donald W.	4	Career
Assoc. General Counsel for Litigation	Webber, Robert D.	4	Career
Asst. Inspector General (Audits)	Randolph, Raymond F.	4	Career
Asst. Inspector General (Investigations)	Reusche, Raymond F.	4	Career
Director of EEO & C	Robinson, George H.	4	Career
Asst. Admin. for External Affairs	Parker, Marshall J.	4	Noncareer
Asst. Admin. for Administration	Jones, Roger H.	4	Career
Director, Computer Sciences	Swope, Paul G.	4	Career
Deputy Asst. Admin. for Administration	Lupkey, Dean F.	3	Career
Director of Personnel	Maas, Joe	4	Career
Deputy Director of Field Management	Prendergast, Albert J.	1	Career
Assoc. Admin. for Finance & Investment	Holloway, Edwin T.	4	Career
Director of Special Guarantees	Armstrong, Arthur E.	4	Career
Director, Portfolio Management	Chambers, Earl L.	4	Career
Deputy Assoc. Admin. Disaster Assistance	Kulik, Bernard	4	Career
Asst. Deputy Admin. Administrator, Disaster Assistance	Lewis, Jean P.	4	Career
Assoc. Admin. for Procurement & Technology Assist.	McDermott, Robert F.	4	Career
Deputy Assoc. Admin. Procurement & Technology Assist.	Browne, Paul R.	1	Career
Assoc. Admin. Management Assist.	Sanders, James C.	4	Noncareer
Asst. Admin., Policy Planning & Budgeting	Garcia, Joe P.	4	Noncareer
Controller	Carver, Harry S.	3	Career

POSITION TITLE	NAME	APPOINTMENT LEVEL	APPOINTMENT STATUS
Deputy Assoc. Admin for Management Assist.	Patrick, John C., Jr.	4	Career
Assoc. Admin., Minority Small Business/Capital Ownership Development	Wright, Robert L.	2	Noncareer
Deputy Assoc. Admin., Minority Small Bus./ Capital Ownership Dev.	Ellison, Carl E.	1	Career
Director, Capital Ownership Development	Luna, Joseph J.	4	Career
Deputy Director, Business Development	Saldivar, Robert H.	2	Career
Regional Administrator Boston	Angevine, James H.	1	Noncareer
Regional Administrator New York	Neglia, Peter P.	1	Noncareer
New York District Director	Tishelman, Harry S.	3	Career
Regional Administrator Philadelphia	Terpeluk, Peter Jr.	1	Noncareer
Philadelphia District Director	Gennetti, William T.	4	Career
Regional Administrator Atlanta	Widemire, Miller A.	1	Noncareer
Deputy Regional Admin.	Messick, Wiley S.	4	Career
Chicago Regional Admin.	Durkin Richard D.	1	Noncareer
Chicago District Office	Smith, John L.	4	Career
Regional Administrator Dallas	Lopez, Reynaldo H.	1	Noncareer
Regional Administrator Kansas City	Powell, William A.	1	Noncareer
Regional Administrator Denver	Suarez, Carlos R.	1	Noncareer
Regional Administrator San Francisco	Castillo, Irenemaree	1	Noncareer
San Francisco District Director	Marvin, Donald J.	3	Career
Regional Administrator Seattle	Hall, Stephen J.	1	Noncareer

VACANT SES POSITIONS

General Counsel
Director of Field Management
Deputy Associate Administrator, Finance & Investment
Deputy Associate Administrator, Financial Assistance
Deputy Associate Administrator, Investment
Deputy Assistant Administrator, Policy, Planning & Budgeting
Director of Business Development
2 Undesignated positions

QUESTION 3: What positions other than the AA for F&I have now been filled in Central Office.

ANSWER: Question Number 2 provides information on all positions that are currently filled.

SBDCs

Of the nineteen SBDC participants, six have contracts or grants which expire at the end of September 1982. Specify the status of each of the other thirteen.

Under the provisions of P.L. 96-302, each state is entitled to a maximum grant based upon the population of the state as compared to the total U.S. population, assuming there is a $65 million program.

Almost every SBDC has told the Committee that the SBA told them the amount of the grant they were to apply for and these amounts are well under the statutory formula. Georgia, for example, with a population of 5.5 million would be entitled to a maximum grant of 2.43 percent of $65 million or $1.58 million. Georgia's grant is $607.3 thousand.

For each SBDC:

QUESTION 1: What date did it enter the program?

QUESTION 2: What SBA funding has it received each fiscal year?

QUESTION 3: How is the amount determined?

QUESTION 4: What is the status of the thirteen SBDCs whose contracts expired December 31, 1981?

ANSWER: The status of the "other 13" SBDC's may be summarized as follows. Four have been issued Cooperative Agreements as of March 1, 1982 at 12:00 noon. The others continue to operate on the basis of a letter agreement pending completion of the full Cooperative Agreement process. It is anticipated that two additional Agreements will be issued by the end of this week. Two of the SBDC's in the "pending" category require substantive changes due to adverse findings from recent reviews. These changes are being affected and continuation of the SBDCs is anticipated.

It is true that SBA has provided guidance to the SBDCs regarding the amount of grant funds likely to be available for a specific performance period. This is necessary in order to obtain maximum utilization of funding.

Preparing a proposal for SBDC operations involves planning and preliminary negotiations with a number of cooperative institutions, consortium members, etc. The more feasible management approach SBA has chosen to use is to provide some reasonable guidance for the planning and preliminary negotiations that results in a proposal that is in the ballpark for funding. We believe this is better management than starting with a huge funding level that later requires an entirely new plan at some funding level less than half the original effort undertaken. If SBA chose the alternative of following this two-step approach, the number of planning efforts would be 4-5 per year which consumes enormous staff time of the SBDC's and SBA.

In response to the four specific, numbered questions, the attached page shows funding for each year, date of entry, and individual status regarding award of agreement (Attachment II). The amount of funds allocated to each school basically follows the population percentage breakout for the state modified by management judgment regarding growth and performance.

Attachment I

The steps to be taken and timetables to effect short and long term improvements are:

I With projected program and budget reductions as proposed for FY/82 and FY/83, reallocation of human resources must be undertaken. The reallocation will be accomplished over next fifteen months and will address the following needs:

1. Increases in field office portfolio management staffs with emphasis on needs related to volume concentrations in certain geographical areas of Disaster Home Loans and farm loans.

2. Increases in staffs of the Office of Data Management in the Central Office in order to meet the separate requirements of accounting and budget control in the Office of the Controller and of the collection arm in the Office of Portfolio Management.

3. Increases in certain staffs of the Controller.

4. Central Office Management plans and Regional and District Office operating plans for the fiscal year will contain specific objectives related to the Debt Collection Plan and shall include (a) appropriate loan making criteria designed to produce better quality of credits (loans) entering the portfolio and (b) quantify measurements in collection efforts designed to motivate and maximize individual collection efforts of field staff members. The planning and development of these objectives began on July 17, 1981, and will be concluded on or before October 1, 1981. Quarterly reviews of results at all levels will be undertaken.

5. The Deputy General Counsel will advise the ten regional counsels to commence a selection process from among SBA's 65 district offices to identify and, in concert with the appropriate United States Attorney, officially designate twelve (12) additional Special Assistant U. S. Attorneys by December 31, 1981. The process will be conducted in a manner previously agreed upon in prior years between the Office of General Counsel (SBA) and the U. S. Department of Justice, Civil Division.

6. Examine contracting out possibilities which might be cost effective and legal, such as collection assistance in the Disaster Home Loan portion of the portfolio. Results may provide rationale to seek budget authority in FY 1983 and beyond. Action to begin now.

II 1. Review various computer generated documents provided to field offices monthly to eliminate duplications and unnecessary reports in order to provide time and manpower relief to computer operations. Complete review by September 30, 1981. Make changes by December 31, 1981.

2. Conduct mutual reviews of certain computer programs and systems to determine what changes can be affected to improve delivery or to eliminate such systems. Complete reviews by December 31, 1981.

3. Initiate action to increase utilization of the ATS data communiations system to replace paperwork trails and delays. Action to commence now.

III 1. To earmark training and travel funds for the specific purpose of upgrading field staff collection competency. To be accomplished by September 30, 1981.

2. To design group training and individual training techniques for collectors. Action to begin now.

3. To conduct training seminars on a periodic basis for collection staffs and supervisors. To begin October 1, 1981.

4. To establish an informal channel of communications between the Central Office directly to and with field office collection staffs. This channel will augment established forms of communications, such as SOP's and Bulletin Items, and will expedite effective collection techniques of particular interest. In addition, it will reinforce high level support and executive emphasis to the entire debt collection effort. Action to begin August 1, 1981.

ATTACHMENT II

SMALL BUSINESS DEVELOPMENT CENTERS

Funding By Fiscal Year

SBDC	FY 1977	FY 1978	FY 1979	FY 1980	FY 1981	FY 1982
Maine	40,000	100,000	165,000	337,500	271,400	272,900
Mass.				210,000	411,000	
Conn.					213,500	
N. J.	70,000	170,000	300,000	349,500	524,100	450,000
Penna.			150,000	24,700	856,054	857,904
D. C.	40,000 1/	120,000 1/	135,000 1/	337,500	265,350	266,325 3/
G. A.	40,000	130,000	290,250	349,500	716,700	652,400
Fla.	40,000	80,000	154,750	357,500	1,083,583	1,089,833
S. C.			40,000	337,500	329,675	310,675 3/
Ala.				257,500	424,520	
Miss.					224,525	
Ky.					224,900	
Wisc.			40,000	349,500	583,600	585,300
Minn.			150,000	24,700	350,675	353,975
Ark.			113,359	24,700	290,650	291,150
Mo.	40,000	130,000	290,000	300,000		
Nebr.	40,000	110,000	250,000	337,500	357,875	310,675 3/
Iowa					237,825	
Utah			150,000	24,700	272,675	274,075
Cal Poly	40,000	90,000	142,500	142,500		
Chicago	40,000	90,000	157,500	157,500		
Wash.			150,000	24,700	420,775	491,608 3/
TOTAL	390,000	1,020,000	2,678,359	3,947,000 2/	8,069,382	6,206,820

1/ Includes 7(j) funding of $40,000, $120,000, and $110,000 respectively.
2/ Additional amount of $373,370 was contracted with the University of Georgia for CQQI.
3/ Contracts have been issued.

ADDITIONAL RESPONSES TO CONGRESSMAN MCDADE'S
QUESTIONS ON THE FISCAL YEAR 1983
CONGRESSIONAL BUDGET SUBMISSION

QUESTION 1: You state that the principal reasons for the decline in loan volume are the high interest rates and the current economic conditions.

A. Is it reasonable, therefore, to assume that a recovery in the economy which includes a significant reduction in interest rates would lead to greatly increased demand for guaranteed loans?

B. If there is a greatly increased demand during FY 1983, would the SBA request supplemental loan guarantee authority.

ANSWER: A. Yes, we believe that would be the case. We think it would depend upon the shape of the recovery. If it is sound and gradual, there would certainly be a gradual, but solid, increase in demand. It is unlikely that recovery will blossom overnight and demand will boom at once.

B. At the current rate of usage, it does not appear that even a great increase in demand would necessitate supplemental guaranty authority. It is our belief that under our current loan quality guidelines, sufficient guaranty authority has been requested to provide assistance to all qualified applicants.

QUESTION 2: Could you provide the Committee with some details regarding SBA's outreach efforts which are designed to increase minority participation in the guaranteed loan program?

ANSWER: At this point our principal efforts will involve continuing contact with private lenders to assure that they are aware of the Administration's desire to provide assistance to minority borrowers and that adequate funds are available. In addition, we intend to continue to emphasize this desire with Agency staff to ensure appropriate consideration is afforded all requests for minority assistance.

QUESTION 3: On page 6 of your statement, and in response to the Chairman's written questions, you state that the proposed personnel reductions will not

prevent you from maintaining current program delivery levels. You say that management improvements and increased private sector participation are expected to overcome these reductions. Can you cite some specific examples of management improvements which have been taken (or are planned) in the areas of management assistance, advocacy, and data and management services?

ANSWER: The Small Business Administration is in the process of realigning all of its personnel resources to provide the small business community the most efficient and effective service possible within the current ceiling limitations.

Management Assistance - We are intensifying our efforts to encourage private sector participation through all the management assistance efforts, including SCORE/ACE, professional and trade associations, Chambers of Commerce and others. We have recently designated, within each district office, a "Private Sector Officer" who will be responsible for interfacing and maintaining positive relationships to ensure increased participation. Each District Director has been asked to make additional contacts with the private sector to encourage their participation. Additionally, within the past two months we have made written contact with 300 professional and trade associations to encourage/request their increased participation.

Also, through the SCORE/ACE volunteer program we are establishing more effective management controls and procedures. All new volunteers will be asked to commit a stated number of hours of effort. Each volunteer will be given a provisionary membership for 90 days, at which time they will be evaluated and either dropped from the program or given full membership. In addition, Central Office officials have delegated more responsibility to the regional and district offices in dealing with volunteers.

Advocacy - Current management improvements include plans to combine two major functions into one unit and streamline the Economic Research Division by eliminating one branch. With increased experience with the Regulatory Flexibility Act (P.L. 96-354) and the Administrations policy to control the rate of growth of regulations, we anticipate significant increased productivity.

Date and Management Services - We are anticipating the purchase of new peripheral equipment (tape and disc) that will eliminate downtime and inefficient usage of computer resources. Through increased efforts toward redesigning major program systems, we anticipate substantial resource savings. Through these streamlining efforts, along with the completion and expansion of the Small Business Administration Data Communications System (SBADCS), we anticipate significant savings in resources and increased efficiency and effectiveness.

QUESTION 4: A. How much in additional disaster loan demand would be created if the interest rates for disaster loans were reduced by a percentage point?

B. Can you break this figure down into the four categories of disaster borrowers:

creditworthy and non-creditworthy homeowners

creditworthy and non-creditworthy businesses

ANSWER: We have no way of estimating with any certainty the amount of additional disaster loan demand that would be created if the interest rates for disaster loans were reduced by a percentage point. The disaster home loan interest rate has increased from 3 percent to 16 percent for those with credit elsewhere, and to 8 percent for those without credit elsewhere with the passage of P.L. 97-35. Since that time, these rates have only varied to 15 1/4 percent and 7 5/8 percent, respectively. We have very little experience with either of the latter rates and no disaster loan experience with rates in between the 3 percent and the 16 percent levels.

A sampling shows that during FY 1981, 45 percent of the disaster loan applications given out by SBA were actually filed with SBA. For disaster declarations during FY 1982 (with an incidence date subsequent to August 13, 1981), the comparable return rate has fallen to 35 percent. However, it must be noted that the actual numbers involved in the latter category are very limited, that some of the post

August 13 disasters are still open, and that there may be many economically related reasons for this reduction.

With respect to 4B, it should be noted that the characterization of loans as "creditworthy" or "non-creditworthy" is erroneous. Any applicant who is found "non-creditworthy" will not be given a loan. Repayment ability must be present in every case. The test of whether credit is available elsewhere, required by the statute, is made by SBA upon consideration of all the factors presented in the application after the application has been filed.

QUESTION 5: A. What is the policy rationale for SBA's decision not to approve any pollution control bonds which are planned as tax exempt?

B. What would be the budget impact of reversing that decision?

ANSWER: A. The decision to permit guarantees of taxable financings only, as of January 1, 1982, is part of the President's initiative to reduce credit intervention activity by the Federal government. Further, SBA believed that taxable guarantee authority would permit the program to operate at a viable level in relation to demand and the cost differential appeared to be reasonable based on prevailing interest rates at the time of the decision.

B. Budget impact would be in the form of lost tax revenue to the Treasury Department. There would be no budget impact to SBA at the present authorized guarantee levels for FY 1982 and FY 1983 which appear to be reasonable in relation to anticipated demand.

QUESTION 6: What is the ratio of disasters declared to the number of requests for disaster declaration for 1981? How does this compare with prior years?

ANSWER:

FY 82 (To Date)	20 Requested	13 Declared	65% Declared
FY 81	119 Requested	79 Declared	66% Declared
FY 80	231 Requested	188 Declared	81% Declared
FY 79	182 Requested	176 Declared	97% Declared
FY 78	172 Requested	151 Declared	88% Declared
TOTAL	724 Requested	607 Declared	84% Declared

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Philadelphia, Pennsylvania
Joseph J. Jones, President
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Miami, Florida

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Hunsberg W. Gary, Secretary
Development Improvement Corporation
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Scott A. Berman, Member of the Board
Lawrence Avenue Development Corporation
Chicago, Illinois
Rosalyn J. Attanasio, Executive Director
South Shore Area Development Company
Chicago, Illinois

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San Antonio, Texas
J. A. Garrett, President
Texas Capital Development Company
Cedar Park, Texas

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Des Moines, Iowa
J. Morris Orr, Executive Director
Kansas City Corporation for Industrial Development
Kansas City, Missouri
Joel D. Seigel, President
St. Louis County Local Development Company
St. Louis, Missouri

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Western Slope Economic Development Company
Grand Junction, Colorado

Region IX
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Bruce Nes, President
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Calexico, California
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Hanford, California
Richard Bayer, Executive Vice President
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Arthur M. Goodman, President
San Diego County Local Development Corporation
San Diego, California
Ben C. Hill, Jr., President
Kendall Bass, Executive Director
Tucson Local Development Corporation
Tucson, Arizona

Region X
John Peeke, Executive Director
Evergreen Community Development Association
Seattle, Washington

March 2, 1982

The Honorable Parren Mitchell
House Small Business Committee
U. S. House of Representatives
Washington, D.C. 20515

RE: SBA's Section 503 Certified Development Company Program

Dear Mr. Chairman:

NADCO is the professional trade association of the nation's Section 503 Certified Development Corporations -- such as the Baltimore Economic Development Corporation (BEDCO) in Baltimore.

Enclosed is our statement in support of the higher funding levels for the 503 program for both fiscal year 1982 and 1983.

As you know, small business is an important source of new jobs in the economy and, now more than ever, these programs should be expanded, not cut back, in order to create permanent private sector jobs -- particularly in high unemployment areas.

We look forward to working with you.

Sincerely,

Allen Neece

Allen Neece, Jr.
Washington Representative

Enclosures

cc: Bernard Berkowitz, BEDCO

NATIONAL ASSOCIATION OF DEVELOPMENT COMPANIES
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JOHN SOWER
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ALLEN NEECE, JR.
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Tucson, Arizona

Region X
John Pasha, Executive Director
Evergreen Community Development Association
Seattle, Washington

GROWTH CAPITAL FOR SMALLER BUSINESS
A NATIONAL ECONOMIC REVITALIZATION STRATEGY
SBA'S NEW 503 PROGRAM

Statement

John Sower
Washington Director, National Development Council and
Incorporating President, National Association of
Development Companies (NADCO)

Congressman Parren Mitchell, Chairman
Small Business Committee
U.S. House of Representatives
Washington, D.C.

March 2, 1982

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GROWTH CAPITAL FOR SMALLER BUSINESS

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GROWTH CAPITAL FOR SMALLER BUSINESS

A NATIONAL ECONOMIC REVITALIZATION STRATEGY

SBA'S NEW 503 PROGRAM

I. THE ISSUES

A. Introduction

Our topic today is SBA's new Section 503 Certified Development Company Program — an important new tool to help smaller businesses increase their capital investment and thereby make a dent in the federal budget deficit by both paying more taxes and creating jobs which reduce unemployment payments.

This presentation will cover "why" the 503 program was created and "why" it is important.

I wear two hats as I speak today — first as Washington Director of the National Development Council, a private, nonprofit organization sometimes known as "economic development investment bankers." Over the past four years, we have helped 75 local communities to organize and implement their economic development financing programs creating $2.0 billion of capital investment in 3,000 small and medium-sized businesses and creating over 130,000 permanent, private sector jobs.

We have revolutionized the local economic development financing business by incorprating rigorous private sector management techniques and a network of financially skilled loan packagers in the nation's major cities. We have helped to institute "hard" policies of providing long-term, fixed asset financing for growing, healthy businesses to create permanent jobs rather than the "soft" money-losing policies of providing stop-gap aids to failing, marginal firms or high-risk start-ups.

My second hat is as unpaid Incorporating President of NADCO — the National Association of Development Companies — a new professional trade association representing the 172 Section 503 Certified Development Companies in local communities across the country.

B. The Economy

1. Introduction

We all know the state of the economy — we are officially in a recession. The tax reductions are just starting and more spending cutbacks are coming. Nonetheless, the pressures of both inflation and interest rates continue. Officials are now talking about an annual federal deficit for Fiscal Year '82 of nearly $100 billion.

2. Overlooked Small Business — Britain

The March 22, 1981 issue of the Miami Herald reported on a study of Britain's economy by Professor Allen Meltzer of Carnegie Mellon University, and states, "The most disturbing of Meltzer's findings about Britain is the failure of Thatcher's tax cuts to produce a spurt of investment."[1]

I'm no great student of the English economy but I am not surprised, as the large percent of their economy consists of government owned monopolies or large corporations supported directly or indirectly by the national government that don't pay much taxes — thus would not be much affected by the change in the tax rate. It is as if we had nationalized and then subsidized W. T. Grants, Chrysler, Amtrak and every other major corporation that has had problems — plus a hundred more.

The October 3rd issue of the Economist had a section on the American economy entitled "Oh, For a Burst of Growth." It stated, "A dash of growth, of course, would work wonders for the President's arithmetic, by cutting outlays and increasing tax revenues."[2] The same issue had a long article about the dynamic growth of smaller business in the English economy in the past decade — despite the adverse economic conditions in that country.

Interestingly, that issue of Economist missed the point — like a trout fisherman who doesn't see the fish swimming at his feet. An important source of new growth and investment in both their economy and ours is smaller business. Even through aggregate economic statistics show a recession with high unemployment and declining industries such as automobiles and steel, many smaller business sectors are booming — particularly those in the newer technologies such as electronics, energy, medicine and computers. Smaller businesses are rapidly creating new jobs, developing new technologies and generating tax revenues in hard-pressed communities.

Thus, a logical policy conclusion would seem to be to aggressively stimulate the growth and investment of smaller businesses, i.e., support your winners instead of your losers. We ought to be aggressively helping expanding, successful smaller business. Unfortunately, smaller business has made it in rhetoric thus far, but not in terms of hard policy — certainly in England and perhaps in our own country.

3. Tax Cuts and Small Business

Tax cuts and tax credits help all businesses, as some of the small business groups have pointed out, they really don't stimulate as much capital formation for smaller businesses which are in lower tax brackets and are less capital intensive. Moreover, tax cuts do not help new businesses nor provide the steady infusion of new capital that is needed in all growing businesses — both large and small.

Tom Richmond, Washington Editor of Inc. magazine, stated in an October 1981 editorial entitled "Why Small Business Lost on the Tax Bill," "If...you take the position that a healthy economy, while necessary, is not

by itself sufficient to insure accelerated growth in a declining small business sector — then small business didn't fare very well."[3]

David Stockman is reputed to have said, "I've never believed that just cutting taxes alone will cause output and employment to expand."[4]

I disagree. I think the President is right — but that it is just a matter of time — although unfortunately, it may take quite a bit of time.

As evidence, I suggest we look at the venture capital industry. A recent Business Week article stated, "After a veritable drought in venture capital investing before the 1978 capital gains tax cut to 28% from 49%, a near flood of money is rapidly reshaping the field. This year, the pool of funds used to back new inventions, technologies and companies is swelling to $6 billion from $2.8 billion in 1977."[5]

In summary — tax cuts will spur investment — gradually not explosively. In the meantime we need to accelerate the capital formation process in the fast booming smaller business area with policies and programs that provide growth capital for smaller businesses — such as SBICs and Section 503 CDCs.

4. Need for Investment

We are all waiting for the "supply-side surge," the slow-in-coming increase in capital investment by the private sector that will generate empoyment, reduce unemployment payments and increase tax revenues — thus reducing the federal deficit and stimulating the nation's economic growth. However, we also need something more — we need more growth capital for smaller businesses — so that they can move now and lead the way out of this recession.

Growth capital is important in other countries as well — and it is more than just tax cuts. A recent British study on capital formation stated, "There is much evidence to indicate that the much envied economic performances, particularly in West Germany and Japan, are based primarily on the availability of long-term, low cost investment credit to their industries."[6]

The important issue, thus, is to find ways to stimulate more investment capital for the growing sectors of our economy — by different methods including tax cuts, reduction of regulations, lower interest rates and more growth capital, particularly for smaller businesses.

C. Importance of Small Business

1. Creation of Jobs

a. The role of small business in creating new jobs in the economy is increasingly realized. In 1979, David Birch of MIT wrote a report entitled "The Job Generation Process" emphasizing the importance of small business in creating new jobs. One conclusion was that "small firms (those with 20 or fewer

employees) generate 66% of all new jobs generated in the U.S."[7]

b. President Reagan, in his April 29, 1981 presentation to the Congress, stated, "Let us not overlook the fact that the small, independent business man or woman creates more than 80% of all new jobs and employs more than half our workforce."

c. George Gilder, one of the Administration's economic advisers, stated in a chapter entitled "The Entrepreneurial Future" in his book Wealth and Povery that "It is small and high technology businesses...that generate most of the employment in America....In addition, small firms provide more than 80% of the jobs for young blacks and other disadvantaged citizens."[8]

2. Technology and Innovation

Small businesses' contribution to innovation and technology development are also increasingly understood. The April 1980 report of the White House Commission on Small Business stated, "Small business has demonstrated incomparable innovative fertility. The National Science Foundation study disclosed that, for every R&D dollar, small companies produce four times more innovation than medium-sized companies and 24 more times innovation than large companies."[9]

They also say, "A study by the Office of Management and Budget shows that more than half the major technological advances of this century originated from individual inventors and small companies."[10]

II. GROWTH CAPITAL GAPS

A. Introduction

1. Definitions

All companies need growth capital — both equity and long-term debt, to finance their normal expansions. Large companies such as AT&T go to Wall Street regularly to sell stocks or bonds. When I was in business school, we learned theoretical formulas for determining whether it was time to raise either debt or equity.

Unfortunately, smaller companies do not have a choice — generally the decision is only of availability, not choice — as there are tremendous growth capital gaps for smaller businesses in our economy.

Moreover, the point is usually overlooked or misunderstood under the assumption that banks or the private sector will provide all the capital that a profitable business needs, or that highly publicized computer companies or "gene splicers," that are wooed by private venture capitalists, are typical of the financing stories of all small businesses.

A recent study by California's Department of Economic and Business Development stated, "A recurring concern...is the availability of capital to support the establishment and growth of dynamic small manufacturers."[11]

Furthermore, the January 1981 issue of Inc. magazine reported on a survey of 2,000 small businesses in which the "availability of long-term credit" was the third most important factor (out of 24) to small businesses in 1982.[12]

2. The Need

A growing small business needs long-term debt capital or equity capital for two primary needs:

a. Fixed Assets

Fixed assets, such as land and building, need to be financed by long-term financing, either as debt or equity. Short-term financing of 3-5 years for a new factory building is no more prudent than for a prospective home buyer.

b. Permanent Working Capital

Secondly, growing companies need permanent working capital in the business. A simple example makes the point. A growing company with annual sales of $1.2 million whose customers pay in 30 days needs $100,000 just to finance the receivables. If sales double to $2.4 million, then the company would need an extra $100,000 for expanded receivables — excluding additional capital needs for the cost of work in process. Some very "profitable" companies go bankrupt by growing too fast — due to this reason.

Tax cuts reduce the amount of money taken out of the business, but do not increase the new capital infusion into the business — which is the key need of a growing business.

B. Equity Capital

Growing smaller businesses usually start with equity investments from the founder/entrepreneur. They have difficulties obtaining equity capital for expansion. This section outlines the equity capital alternatives for smaller businesses ranging from informal risk capital from friends and neighbors to Wall Street investment bankers.

There really isn't much equity capital available to begin with. Mr. Reginald H. Jones, former Chairman and Chief Executive Officer of the General Electric Company, stated at the recent annual meeting of the American Council for Capital Formation, "In the decade of the 1960s, new equity provided only 1.5% of corporate cash sources. This grew to 5.6% in the first half of the 1970s but then fell sharply in the last half of the decade."[13] He predicted a figure of 3.4% during the '80s, most of which is for the nation's largest corporations — not growth capital for smaller businesses.

1. Informal Risk Capital

Most businesses start with money invested from the founder or his/her friends or associates. SBA's Office of Advocacy did a study of this source of capital which stated, "Informal investors are difficult to reach — geographically dispersed and tough to identify."[14] They also stated, "...the availability of essential risk capital (venture and equity capital to finance new and growing small firms declined steadily during the 1970 decade."[15]

2. Venture Capital

Venture capital is a phrase describing a variety of people and organizations including SBICs, private investors, corporations, etc. Venture capitalists are generally private sector investors looking for the "cream of the crop," the fast growing, most potentially profitable businesses. They do not finance the normal expansion needs of most smaller businesses. The September 1981 issue of Inc. magazine stated, "Organized venture capital will have little impact on the expansion capital needs of the vast majority of small businesses."[16]

In a section entitled "Expansion Capital: The Critical Issue," he stated, "Only a tiny fraction of the half million businesses started in the U.S. each year promise the kind of returns on invested money venture capitalists need."[17] In the same issue, Mr. Morton Collins, President of the National Venture Capitalists Association, states, "We are in the business of financing losses, not plant and equipment,"[18] i.e., venture capitalists are interested in fast growing start-ups and not moderate expansions needing plant and equipment.

David Brophy, Professor of Finance at the University of Michigan in Ann Arbor, Michigan, commented on Michigan's depressed economy and stated, "I compared Ann Arbor to Boston and Palo Alto because those are the two points of reference for technology-based industry. And as I visited there and talked with people, it appeared financing was the key element. Without local access to venture and growth money, the businesses just don't grow."[19] He cited the key difference between Michigan and Boston or Palo Alto respectively was that "Michigan's technology-based firms had to go out of the state to raise more of their venture capital."[20]

3. Investment Bankers

Investment bankers are the largest source of equity capital for large corporations, however they do not provide substantial equity capital for growing small businesses. An August 1981 study done by the SEC and SBA entitled "The Role of Regional Broker-Dealers in the Capital Formation Process: Underwriting, Market-Making and Securities Research Activities," pointed out that although the minimum initial public offering underwriting criteria of regional broker dealers was less than for national broker dealers, their standards still were too large for smaller businesses as their minimum dollar volume for an underwriting was $2.1 million, the minimum annual revenues for a client business was $4.4 million, the minimum net worth for a potenial business was $1.7 million, the minimum net profit was $600,000 and the minimum number of years incorporated was three years."[21]

The point is further made in a recent publication of the Donaldson, Lufkin and Jenrette Investment Banking concern where it describes its particular expertise in specific sectors including energy and emerging growth companies such as the computer, electronics or medical technology areas.[22]

4. Summary

Summarizing equity capital, although there are many players in equity and venture capital, most of them are chasing the cream of the crop and according to Inc. Magazine of September 1981, "The supply of expansion capital for small business has never been adequate in recent years and is less so today. The innovation and expansion capital gap will continue to be the critical problem for small business."[23]

C. Debt Capital

It is also difficult for most growing, profitable firms to obtain long-term debt capital for expansion.

1. Financial Institutions

None of the financial institutions are in the market for providing long-term debt capital for growth businesses.

a. Banks — All small businesses have bankers, yet bankers are short-term lenders — particularly in today's money market. Tax-exempt industrial revenue bonds, mostly bank loans in disguise, are helpful as they do reduce the interest rate.

b. Savings Institutions — Savings institutions were created to finance residential development, and in today's money market they are inactive.

c. Insurance Companies and Premium Funds — Insurance companies and pension funds are the primary source of long-term capital in the economy, however, they prefer larger projects — over $1 million.

Consequently, there is a long-term loan gap for smaller businesses in our economy.

2. First National Bank of Boston Study

The Council for Northeast Economic Action, an affiliate of the First National Bank of Boston, published a study in February 1981 entitled "An Empirical Analysis of Unmet Demands in Domestic Capital Markets in Five U.S. Regions."[24] Their survey was mailed to 30,000 business firms selected by five major banks, and the results confirm the growth capital gaps for smaller businesses. They concluded that there is a long-term credit gap for smaller businesses and that there may be as many as 50,000 viable smaller firms that have been unable to raise funds in the capital market.

3. Neighborhood Business Revitalization Program

The National Development Council's Neighborhood Business Revitalization program offers further evidence of the long-term debt capital for smaller businesses. In a four-year time period, the National Development Council was able to work in sixty cities and obtain long-term debt financing for 3,000 small and medium-sized businesses totaling $2.1 billion and creating over 130,000 private sector jobs. This figure really represents the tip of the iceberg rather than any saturation of the demand for long-term credit for viable businesses nationwide.

4. Small Business Investment Companies

Small Business Investment Companies (SBICs) are a tremendously important source of growth capital and include approximately 350 SBICs licensed by the SBA which in turn lend money to SBICs at preferred rates. SBICs have private investment from their owners and long-term debt from SBA. However, the report of the White House Commission on Small Business was concerned about the use of debt by SBICs and stated, "SBICs and minority enterprise SBICs in recent years have tended to relend their money to small companies at higher interest rates instead of investing in equity."[25]

5. Certified Development Companies

A newer program, designated specifically to provide long-term, subordinate debt for the fixed asset expansion needs of growing smaller businesses, is SBA's Section 503 Certified Development Company program. This program has been operative for approximately 10 months and has met tremendous demand for long-term debt capital by growing small businesses. In that time period, over 200 communities submitted applications to participate and 260 loans have been approved totaling approximately $40 million.

III. SUMMARY AND CONCLUSIONS

A. Summary

The growth capital needs of smaller businesses can be summarized by visualizing a pyramid in three tiers: Venture Capital, Risk Capital and Expansion Capital.

1. Venture Capital

The top layer is the cream of the crop of the venture capital business — very high risk, very few deals, very private sector and very high reward if you hit it right.

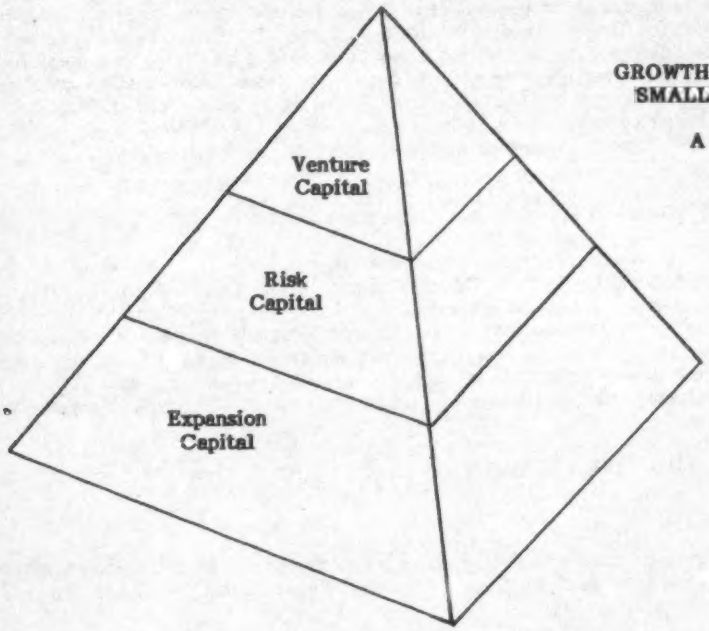
2. Risk Capital

The next "tier" of the pyramid might be called risk capital and includes both equity and debt investments by private investors for smaller businesses. Risk capital is predominantly private sector, although SBICs receive government guaranteed debentures. Investors in these businesses

do seek long-term growth — although not as risky perhaps as venture capital. The risk capital tier is larger than venture capital.

3. Expansion Capital

The third and bottom tier of the growth capital pyramid could be labeled "expansion capital," and is the area for the new SBA Section 503 program. CDCS, or Certified Development Companies, are public/private partnerships and are very important in the long-term creation of jobs in growing smaller businesses throughout the country. These long-term, fixed asset loans to expanding, profitable companies are not risky, and there isn't sufficient reward to invite venture or risk capital. This bottom tier of the pyramid is by far the largest.



GROWTH CAPITAL FOR SMALLER BUSINESS

A Pyramid

Tier	Risk	Reward	Volume of Business	Private or Public $
Venture Capital	Very High	Very High	Very High	Totally Private
Risk Capital	Moderate	Moderate	Moderate	Mostly Private
Expansion Capital	Low	Low	Very Many	Public/Private

B. Cost Effectiveness

The SBIC and CDC programs indirectly use long-term government debt, which, contrary to common knowledge is declining relative to the GNP. The October 1981 issue of the newsletter from the American Council for Capital Formation quotes Professor Benjamin J. Friedman, Harvard Professor of Economics, in a study completed by the National Bureau of Economic Research, "Except only for 1975-76 and 1980, the Federal government has reduced its debt ratio every year since 1953."[26]

Also, the February 1, 1982 issue of Forbes states, "Fears that Federal borrowing will crowd out private borrowing are greatly exaggerated."[27]

The use of long-term government debt to leverage private debt and create permanent, private sector employment in expanding, successful small and medium-sized businesses must stand the test of cost effectiveness. What are the real costs of job creation in CETA, public service job programs, welfare, crime, supplemental unemployment insurance, etc.?

The Neighborhood Business Revitalization demonstration program created 132,584 jobs in 2,943 small and medium-sized businesses resulting from financing of $2.1 billion of capital investment. This results in one job created for each $15,616 of investment of which $13,199 is private capital and $2,417 is from the government. Hence, one permanent job can be created with a cost of $2,417 — which gets repaid with interest.

This is far more cost effective than the other programs which require $10,000-20,000 per year for each job — each year!

C. Conclusion

The November 2nd editorial of Business Week stated, "The facts are making it distressingly but unmistakably clear that the economy is not responding as hoped."[28] The supply side surge is slow in coming.

Our policy conclusion is as follows: All companies need capital investment to grow, to create jobs, to pay taxes and to increase the competitiveness and productivity of the American economy. Smaller businesses are a primary source of that growth and job creation but they are not the focus of policy — particularly regarding the availability of growth capital which, as outlined above, is not very available from the wide variety of sources of capital in the American economy.

Statistics from the SBIC, Section 503 CDC and Neighborhood Business Revitalization programs show that policies and programs to create jobs and stimulate the economy are far more cost effective than other employment programs. However, more attention and stronger policies and programs to provide growth capital for smaller businesses are needed. The same is true in Britain. A recent Economist article on the growth of high technology companies in Britain laments, "Many high tech companies have come to grief (or never got off the ground) through lack of finance."[29]

In a chapter entitled "The Imperatives of Growth," George Gilder summarizes, "Those smaller corporations with less access to loans, no access to equity markets...suffer more obviously (from inflation and excessive regulation)."[30]

His policy recommendation is: "If the United States diverts the proceeds of its inflation tax into the creative core of capitalist growth — the new research and industry of the future — both the problem of inflation and the problem of growth will disappear."[31]

Stronger policies and programs providing growth capital for smaller businesses, such as the 503 program, are the essence of that policy.

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FOOTNOTES

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